used to finance the communication), including the date and amount of those donations;

- Disbursements of more than $200, including the name and address of the payee, date, amount and purpose of the disbursement, the name of the federal candidate, and the election identified in the communication;
- Total donations received and disbursements made in this report;
- Aggregate disbursements year-to-date;
- The disclosure date (*i.e.*, the date when the communication was first publicly distributed); and
- The following statement: ''Under penalty of perjury, I certify that this report is true, correct and complete.'' followed by the name/signature of the person making that statement and the date.[2]

Dated: November 22, 2002.

David M. Mason,

Chairman, Federal Election Commission.

[FR Doc. 02–30265 Filed 11–27–02; 8:45 am]

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NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 702, 741 and 747

Prompt Corrective Action

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: Pursuant to Congressional mandate, the National Credit Union Administration (NCUA) adopted a comprehensive system of prompt corrective action consisting of minimum capital standards and corresponding remedies to restore the net worth of federally-insured credit unions. After six quarters of implementation, the NCUA Board issued a proposed rule consisting of revisions and adjustments intended to improve and simplify the system of prompt corrective action. As revised to reflect public comments, the NCUA Board now issues a final rule incorporating these improvements.

DATES: Effective January 1, 2003.

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The following acronyms are used throughout:

CUMAA Credit Union Membership Access Act
DSA Discretionary Supervisory Action
MBL Member Business Loan
MSA Mandatory Supervisory Action
NWRP Net Worth Restoration Plan
OCA Other Corrective Action
PCA Prompt Corrective Action
RBNW Risk-Based Net Worth
RBP Revised Business Plan
RMC Risk Mitigation Credit

Throughout the Supplementary Information section, citations to part 702 refer to the current version of 12 CFR 702 *et seq.* (2002) and are abbreviated to the section number only.

A. Background

1. Development of Part 702

In 1998, Congress enacted the Credit Union Membership Access Act (''CUMAA''), Pub. L. 105–219, 112 Stat. 913 (1998). CUMAA amended the Federal Credit Union Act (''the Act'') to require NCUA to adopt by regulation a system of ''prompt corrective action'' (''PCA'') consisting of minimum capital standards and corresponding remedies to improve the net worth of federally-insured ''natural person'' credit unions. 12 U.S.C. 1790d *et seq.* In February 2000, the NCUA Board adopted part 702 and subpart L of part 747, establishing a comprehensive system of PCA that combines mandatory supervisory actions prescribed by statute with discretionary supervisory actions developed by NCUA, all indexed to five statutory net worth categories. 65 FR 8560 (Feb. 18, 2000).

Subpart A of part 702 consists of standards for calculating a credit union's net worth and classifying it among five statutory net worth categories. 12 CFR 702.101–108. Also included in subpart A is a separate risk-based net worth (''RBNW'') component that applies to non-''new'' credit unions, § 702.102(a)(1)–(2), that satisfy minimum RBNW and asset size requirements, § 702.103, and whose portfolios of assets and liabilities carry above average risk exposure. § 702.104; 65 FR 44950 (July 20, 2000). Subpart B combines mandatory and discretionary supervisory actions indexed to the five categories, as well as PCA-based conservatorship and liquidation. §§ 702.201–206. Subpart C consists of a system of PCA for ''new'' credit unions. §§ 702.301–307. Subpart D prescribes reserve accounts, requirements for full and fair disclosure of financial condition, and prerequisites for paying dividends consistent with the earnings retention requirement in subpart B. §§ 702.401–403. In addition to these substantive provisions, subpart L of part 747 established an independent review process allowing affected credit unions and officials to challenge PCA decisions. 12 CFR 747.2001 *et seq.* (2000).

Part 702 and subpart L of part 747 were effective August 7, 2000, and first applied to activity in the fourth quarter of 2000 as reflected in the Call Report for that period. The RBNW component of part 702 was effective January 1, 2001, and first applied (for quarterly Call Report filers) to activity in the first quarter of 2001 as reflected in the Call Report for that period.[1]

At the conclusion of the initial PCA rulemaking process, the NCUA Board directed the ''PCA Oversight Task Force'' (a working group consisting of NCUA staff and State regulators) to review at least a full year of PCA implementation and recommend necessary modifications. 65 FR at

[2] Submission of false, erroneous or incomplete information may subject the person signing this report to the penalties of 2 U.S.C. 437g.

[1] Part 702 has since been amended twice—once to incorporate limited technical corrections, 65 FR 55439 (Sept. 14, 2000), and once to delete sections made obsolete by the adoption of a uniform quarterly schedule for filing Call Reports regardless of asset size. 67 FR 12459 (March 19, 2002).

44964. This final rule is the result of those recommendations, as modified to reflect public comments. The final rule takes effect January 1, 2003, and first applies to activity in the first quarter of 2003 as reflected in the Call Report for that period.

2. Where Credit Unions Stand Today

a. *Net worth classification.* As of June 30, 2002, federally-insured credit unions are classified as follows within the PCA net worth categories:

TABLE A -- NET WORTH CLASSIFICATION OF NON-"NEW" FICUS

Statutory net worth category	*Net worth ratio*	*# of non-"new" FICUs*	*Percent of all non-"new" FICUs*
"Well Capitalized"	7% or greater	9382	96.49%
"Adequately Capitalized"	6% to 6.99%	231	2.38%
"Undercapitalized"	4% to 5.99%	83	0.85%
"Significantly Undercapitalized"	2% to 3.99%	17	0.17%
"Critically Undercapitalized"	Less than 2%	10	0.10%

TABLE B -- NET WORTH CLASSIFICATION OF "NEW" FICUS

"New" net worth category	*Net worth ratio*	*# of "new" FICUs*	*Percent of all "new" FICUs*
"Well Capitalized"	7% or greater	45	49.45%
"Adequately Capitalized"	6% to 6.99%	12	13.19%
"Moderately Capitalized"	3.5% to 5.99%	20	21.98%
"Marginally Capitalized"	2% to 3.49%	8	5.49%
"Minimally Capitalized"	0% to1.99%	7	7.69%
"Uncapitalized"	Less than 0%	2	2.20%

b. *RBNW requirement.* As of June 30, 2002, 448 federally-insured credit unions—4 percent of the total—were required to meet an RBNW requirement. Of these, 446 met the requirement using the ''standard calculation.'' § 702.106. The two that failed under the ''standard calculation'' succeeded in meeting their RBNW requirements using the ''alternative components.'' § 702.107. To date, no credit union has completely failed its RBNW requirement, and no credit union has applied for a ''risk mitigation credit.'' § 702.108.

3. Comments on Proposed Rule

On June 4, 2002, NCUA issued a proposed rule consisting of revisions and adjustments intended to improve and simplify the system of PCA. 67 FR 38431 (June 4, 2002). By the close of the comment period for the proposed rule, August 5, 2002, NCUA received 26 comment letters. Comments were received from seven federal credit unions, four state credit unions, eight state credit union leagues, two credit union industry trade associations, an association of state credit union supervisors, two banking industry trade associations, and a Federal Home Loan Bank. Nearly all of the comments supported the series of proposed revisions and adjustments to part 702.

This rulemaking will not address the few comments that suggested modifications to part 702 that exceed the scope of NCUA's statutory authority or that are completely unsupported. Comments on the concept of ''safe harbor'' approval of a net worth restoration plan are addressed in a separate proposed rule found elsewhere in this volume of the **Federal Register**. All other comments are analyzed generally in section B. below.

B. Section-by-Section Analysis of Final Rule

Part 702—Prompt Corrective Action

1. Section 702.2—Definitions

a. *Dividend.* Subpart D of part 702 sets various restrictions and requirements regarding the payment of dividends to members. §§ 702.403, 702.401(d), 702.402(d)(5). To extend these restrictions and requirements to interest that many State-chartered credit unions pay on shares and deposits, the proposed rule introduced a definition of ''dividend'' that included ''a payment of interest on a deposit by a State-chartered credit union.'' 67 FR at 38433. While one commenter supported the definition as proposed, two others pointed out that State-chartered credit unions pay interest on non-share deposits pursuant to a contractual obligation, and that restricting the payment of interest would cause a credit union to breach its deposit contract with the member. By comparison, dividends paid on shares entail no such contractual obligation. NCUA concurs with the commenters' point. Accordingly, the final rule omits the proposed definition of ''dividends'' and, further, eliminates the reference to ''interest'' in the discretionary supervisory action (''DSA'') restricting the payment of dividends. §§ 702.202(b)(3), 702.203(b)(3), 702.204(b)(3). As a result, the term ''dividends'' as used in part 702 excludes only those payments on shares and deposits that meet a statutory or other legal definition of contractual interest, regardless of the label a credit union gives to such payments.

b. *Senior executive officer.* Part 702 neglected to define who is a ''senior executive officer'' for purposes of the DSAs that authorize dismissing ''a director or senior executive officer,'' §§ 702.202(b)(7), 702.203(b)(8), 702.204(b)(8); hiring of a ''qualified senior executive officer,'' §§ 702.202(b)(8), 702.203(b)(9), 702.204(b)(9); and limiting compensation paid to a ''senior executive officer,'' §§ 702.203(b)(10), 702.204(b)(10). *See also* 12 CFR 747.2004(a) (review of dismissal of senior executive officer). To correct this oversight, NCUA proposed incorporating by reference the definition of a ''senior executive officer'' in 12 CFR 701.14(b)(2). 67 FR at 38433. Apart from a misquotation in the preamble to the proposed rule, the sole commenter supported the proposed definition. Accordingly, the final rule adds a new subsection (i) to § 702.2 that incorporates by reference the definition of ''senior executive officer'' in 12 CFR 701.14(b)(2).

c. *Total assets.* The ''average quarterly balance'' definition of ''total assets'' was ambiguous as to whether the phrase ''[t]he average of quarter-end balances of the four most recent calendar quarters,'' § 702.2(j)(1)(i), refers to the four consecutive quarters *preceding* the then-current quarter, or to the then-current quarter *plus* the preceding three consecutive quarters. The proposed rule revised the definition to adopt the latter meaning. 67 FR at 38433. Apart from a misquotation in the preamble to the proposed rule, the two comments on the definition favored the latter meaning. Accordingly, the final rule redefines the ''average quarterly balance'' as the average of quarter-end balances of ''the current and three preceding calendar quarters.'' In addition, the final rule deletes the reference to semiannual first and third quarter Call Reports from the ''quarter end balance'' definition of ''total assets,'' § 702.2(l)(1)(iv), to reflect the adoption of a uniform quarterly schedule for filing Call Reports. 67 FR 12457 (March 19, 2002).

2. Section 702.101—Measures and Effective Date of Net Worth Classification

For nearly all credit unions, the effective date of net worth classification is the ''quarter-end effective date''—''the last day of the calendar month following the end of the calendar quarter.'' § 702.101(b)(1). Occasionally, however, an interim effective date between quarter-ends applies instead because ''the credit union's net worth ratio is recalculated by or as a result of its most recent final report of examination.'' § 702.101(b)(2). This typically results when an NCUA examination that takes place after the quarter-end effective date discloses that the credit union erred in calculating its net worth ratio and the corrected ratio puts it in a different net worth category. In that case, the date the credit union receives the final examination report becomes the new effective date of classification to the proper net worth category.

Several flaws have made it difficult to implement subsection (b)(2). First, it extended to instances where there was no error or misstatement in calculating net worth, but rather, data or conditions simply had changed since the date of the Call Report (which would be reflected in the next quarter's Call Report). Second, notice to the credit union to correct its net worth ratio had to await the ''most recent report of final examination'' even when an earlier supervision contact disclosed a calculating error or misstatement. Third, postponing such notice may deprive the credit union of the opportunity to take corrective action sooner. To rectify these flaws, the proposed rule revised subsection (b)(2) to define the effective date of classification to a ''corrected net worth category'' as ''the date the credit union receives subsequent written notice . . . of a decline in net worth category due to correction of an error or misstatement in the credit union's most recent Call Report.'' 67 FR 38434. NCUA received three comments on this section, all favoring these revisions. Therefore, the final rule adopts them as proposed.

3. Section 702.106—Standard Calculation of RBNW Requirement

The proposed rule suggested no modifications to the standard component for ''member business loans outstanding'' (''MBLs''). § 702.106(b). However, one commenter contended that the 12.25 percent risk-weighting threshhold in that component was arbitrarily based on CUMAA's restriction on member business lending, 12 U.S.C. 1757a(a)(2), and proposed that the threshhold be increased to 25 percent. After considering this suggestion, the NCUA Board has determined that the existing 12.25 percent threshold warrants reconsideration in connection with its review of the current MBL regulation, 12 CFR 723. Pending reconsideration, a credit union has two alternatives if it finds that the 12.25 percent threshhold distinguishes risk weightings among MBLs imprecisely. First, to resort to the corresponding alternative component for MBLs, § 702.107(b), which measures finer increments of risk among fixed- and variable rate MBLs. And second, to seek a risk mitigation credit, § 702.108, to moderate the impact of the standard risk-weightings. Accordingly, the existing 12.25 percent threshold is retained at this time.

4. Section 702.107—Alternative Components for Standard Calculation

a. *Alternative component for long-term real estate loans callable in 5 years or less.* For long-term real estate loans, part 702 features both a ''standard component'' and an ''alternative component'' for the RBNW calculation. §§ 702.106(a), 702.107(a). The longer the maturity of the loan, the greater the interest rate risk and credit risk exposure, justifying a correspondingly greater risk-weighting. *See* 65 FR at 44960–44961. Both components scheduled loans by contractual maturity date regardless whether there is a ''call'' feature permitting the lender to redeem the loan before the maturity date. The NCUA Board declined to propose scheduling ''callable'' loans by ''call'' date, rather than by maturity date, for reasons explained in the proposed rule. 67 FR at 38435. Instead, the NCUA Board suggested than an offsetting risk mitigation credit under § 702.108 was well suited to recognize when a credit union's program and history of efficiently exercising ''call'' options truly mitigates risk.

Six commenters objected that the NCUA Board's position denies them a reduced risk-weighting even though a ''call'' feature gives them the flexibility to shorten the term of real estate loans, thereby mitigating interest rate risk, and credit risk due to deterioration of the borrower's ability to repay or the collateral's value. One commended the ''call'' feature as a risk management tool. Another advocated allowing use of the ''call'' date, in lieu of the maturity date, on a credit union-by-credit union basis. And finally, a commenter recommended categorizing ''callable'' and non-''callable'' loans separately and assigning lower risk weightings to the ''callable'' category to reflect its reduced interest rate risk. In light of these comments, the NCUA Board has reconsidered its position and now recognizes that a ''call'' feature, when exercised in good faith, provides some measure of risk mitigation for real estate loans.[2]

[2] The alternative component for MBLs continues to categorize MBLs by fixed- and variable-rate and then schedules the loans in each category for risk-weighting by remaining maturity. § 702.107(b). The NCUA Board is not scheduling MBLs by ''call'' date at this time out of concern for credit risk upon exercise of the ''call'' feature. However, this issue also may receive further consideration in

Accordingly, the final rule expands the existing alternative component for ''long-term real estate loans'' to add a separate schedule for loans that are ''callable'' within a maximum period of 5 years. § 702.107(a)(2). The schedule consists of three maturity buckets that correspond to the buckets in the non-''callable'' schedule. *See* new Table 5(a) and new Appendixes C in rule text below. A loan that is ''callable'' within 5 years, and that has remaining maturity of less than 5 years, receives the same six percent risk-weighting that the existing alternative component gives to a non-''callable'' loan with a remaining maturity of less than 5 years. A loan that is ''callable'' within 5 years, and that has a remaining maturity of more than 5 years, receives a risk weighting that is two percentage points lower than the weighting for the corresponding non-''callable'' maturity bucket. To qualify for the ''callable'' schedule, the ''call'' feature must be contractually specified in the loan documents and the credit union must maintain records documenting the breakdown of ''callable'' loans by maturity bucket.

b. *Alternative component for loans sold with recourse.* The standard component for loans sold with recourse assigns a uniform risk-weighting of 6 percent to the entire balance, § 702.106(f), regardless whether it includes loans sold with only *partial* recourse against the seller. Since part 702 was adopted, recourse loan activity among credit unions has nearly doubled, and loan programs have emerged that contractually limit the extent of the purchaser's recourse to the seller.[3] Thus, credit unions have gained the ability to cap their credit risk exposure from the sale of recourse loans.

In view of these developments, the proposed rule added a fourth alternative component to § 702.107 that would allow variable risk-weighting according to the actual credit risk exposure of loans sold with a contractual recourse obligation of less than 6 percent. 67 FR at 38434. The proposed alternative component is the sum of two risk-weighting buckets. The first bucket consists of the balance of loans sold with contractual recourse obligations of six percent or greater; it is risk-weighted at a uniform six percent. § 702.107(d)(1). The second bucket consists of the balance of loans sold with contractual recourse obligations of less than six percent; it is risk-weighted according to the weighted average recourse percent of its contents, as computed by the credit union.[4] § 702.107(d)(2); *see* new Table 5(d) and new Appendixes F and G in rule text below. Eight comments addressed the proposed ''alternative component'' for loans sold with recourse, all supporting it. Therefore, the final rule adopts the new alternative component in § 702.107(d) as proposed.

c. *Alternative component for short-term government obligations.* Although the proposed rule did not reference government obligations, a single commenter proposed an alternative component for government obligations with maturity of one year or less. Under the proposal, these obligations, up to a total equivalent to 25 percent of a credit union's total assets, would receive a zero risk weighting. The NCUA Board is unsympathetic to this proposal because the existing standard component for ''investments'' gives a risk-weighting of three 3 percent-half the six percent risk weighting assigned to average risk assets—to government obligations with a maturity of one year or less. § 702.106(c)(1). Government obligations are not completely risk free, as a zero risk-weighting suggests. On the contrary, they carry interest rate risk and transaction risk that justify a three percent risk weighting. Accordingly, the commenter's proposal is not adopted.

5. Section 702.108—Risk Mitigation Credit

Part 702 permits a credit union that fails an applicable RBNW requirement under both the ''standard calculation'' and the ''alternative components'' to apply for a ''risk mitigation credit'' (''RMC''). § 702.108(a). If granted, an RMC will reduce the RBNW requirement that must be met.[5] But NCUA will not consider an application for this relief until after the effective date that a credit union fails its RBNW requirement. *Submission Guidelines* § I.3. This forces a failing credit union to remain classified ''undercapitalized'' while its RMC application is pending, *id.* §§ I.4, I.8, even when it reasonably expects to fail because it either failed or barely passed in a preceding quarter.

To spare credit unions that are genuinely in danger of failing an RBNW requirement from the ''fail first'' prerequisite, the proposed rule allowed them to apply for an RMC preemptively—that is, to apply in advance of the quarter-end so that the credit union receives any RMC for which it qualifies *before* the approaching effective date when it would fail its RBNW requirement. 67 FR at 38434. As revised, § 702.108 would allow a credit union to apply for an RMC at any time before the next quarter-end effective date if on any of the current or three preceding effective dates of classification it has either failed an applicable RBNW requirement, or met it by less than 100 basis points. An RMC granted preemptively would allow a credit union genuinely at risk of failing an RBNW requirement to seamlessly maintain its initial classification as either ''adequately capitalized'' or ''well capitalized.'' The nine commenters who addressed this endorsed the proposed relaxation of the RMC application prerequisites. Therefore, the final rule adopts the revisions to § 702.108 as proposed.

6. Section 702.201—PCA for ''Adequately Capitalized'' Credit Unions

a. *Earnings retention.* The proposed rule identified two flaws in the operation of the quarterly earnings retention requirement that applies to credit unions classified ''adequately capitalized'' or lower. First, that subsection (a) failed to specify that it is the dollar amount of net worth that must increase by the equivalent of 0.1 percent of assets per quarter, not the net worth ratio itself. (Changes in the net worth ratio will not match changes in the dollar amount of net worth unless net worth and total assets were to increase or decrease by exactly the same percentage.) Second, that subsection (a) technically does not allow credit unions to meet the statutory annual minimum transfer of the equivalent of 0.4 percent of total assets *on an average basis* over four quarters. As originally written, that subsection requires that the equivalent of 0.1 percent of assets be set aside in each and every quarter of the year, regardless whether the credit union has set aside more than the quarterly minimum in prior quarters.

To address both flaws, the proposed rule revised subsection (a) to specify that it is the ''the dollar amount'' of net

connection with NCUA's review of the current MBL regulation, 12 CFR.

[3] For example, documentation for the loan sale transaction may provide for recourse in the form of a contractually-specified recourse obligation measured either by a designated dollar amount that is fixed for the life of the loan, or by a designated percentage of the unpaid balance of a pool of loans.

[4] To caluate the ''weighted average recourse percent'' of the bucket of loans sold with recourse <6%, multiply each percentage of contractual recourse obligation by the corresponding balance of loans sold with that recourse to derive the total dollars of recourse. Divide the total dollars of recourse by the total dollar balance of loans sold with <6% recourse to derive the alternative risk weighting. *See* Appendix G in rule text below.

[5] To aid credit unions seeking a ''Risk Mitigation Credit,'' NCUA has released two publications: *Guidelines for Submission of an Application for PCA ''Risk Mitigation Credit''* (NCUA form 8507) *(''Submission Guidelines'')* and *Guidelines for Evaluation of an Application for PCA ''Risk Mitigation Credit''* (NCUA for 8508). The *Submission Guidelines* will be modified to reflect the revisions to § 702.108 adopted in this final rule.

worth that must be increased, not the net worth ratio itself, and to permit the minimum increase to be made ''either in the current quarter, or on average over the current and three preceding quarters.'' None of the commenters addressed these revisions. Therefore, the final rule adopts them as proposed.

b. *Decrease in retention.* Subsection (b) authorized NCUA, on a case-by-case basis, to permit a credit union to increase net worth by an amount that is less than the quarterly minimum (equivalent of 0.1 percent of assets) when necessary to avoid a significant redemption of shares and to further the purpose of PCA. § 702.201(b); 12 U.S.C. 1790d(e)(2). Since the adoption of part 702, however, some credit unions have decreased their quarterly earnings retention, either without seeking NCUA's permission at all, or prior to seeking NCUA's permission, in order to pay dividends as they deem necessary. To prevent unilateral decreases in earnings retention, the proposed rule revised subsection (b) to add the requirement that a request to decrease earnings retention must be submitted in writing no later than 14 days before the quarter end. NCUA would be under no obligation to grant applications submitted after the 14-day deadline expires or after the quarter-end. Further, NCUA would be entitled to take supervisory or other enforcement action against credit unions that either decrease their earnings retention without permission, or persist in failing to timely apply for permission.

Two commenters advocated a more flexible approach—making the application period negotiable, and accepting verbal applications after the deadline, both on a case-by-case basis. The NCUA Board continues to believe that a documented request submitted within a ''bright line'' time frame is necessary for two reasons. First, to give credit unions clear notice of when they must apply for a decrease. Second, to facilitate uniform discipline of credit unions that unilaterally pay dividends without advance permission to decrease their earnings retention. A third commenter objected that a request to decrease earnings retention should not be required when a credit union is operating under an approved net worth restoration plan (''NWRP'') that projects quarterly earnings retention that is less than the minimum. *See* § 702.206(c)(1)(ii). In fact, a separate request for a decrease is not required under these circumstances because, as explained below, earnings retention is effectively subject to quarterly evaluation as a function of the NWRP. For these reasons, the final rule adopts the revisions to subsection (b) as proposed.

c. *Decrease by FISCU.* The requirement to ''consult and seek to work cooperatively'' with State officials when deciding whether a State-chartered credit union may decrease its earnings retention was originally located in § 702.205(c), where it was misidentified as a DSA. Because § 702.205(c) applies only to DSAs, the final rule relocates the ''consult and work cooperatively'' requirement to a new subsection (c) of § 702.201.

d. *Periodic review.* Part 702 provides that a decision permitting a decrease in earnings retention is ''subject to review and revocation no less frequently than quarterly.'' § 702.201(b); 12 U.S.C. 1790d(e)(2)(B). In practice, the ''no less frequently than quarterly'' timetable is too vague to indicate when such a review must take place. To coincide with the quarterly Call Reporting schedule that drives part 702, the proposed rule added a new subsection (d) to require uniform ''quarterly review and revocation,'' except when a credit union classified ''undercapitalized'' or lower is operating under an approved NWRP. NCUA received no comments on this modification.

For ''adequately capitalized'' credit unions (for whom earnings retention is the only MSA), quarterly review is implicit because a request to decrease earnings retention already must be renewed on a quarter-by-quarter basis. However, for credit unions classified ''undercapitalized'' or lower, separate quarterly review would be redundant when an approved NWRP is in place. To be approved, an NWRP must, in addition to prescribing quarterly net worth targets, § 702.206(c)(1)(i), project the amount of earnings retention, decreased as permitted by NCUA, for each quarter of the term of the NWRP. § 702.206(c)(1)(ii). Typically, approved NWRPs permit decreases in earnings retention extending for successive quarters over the term of the plan. These decreases are effectively subject to quarterly review and revocation as a function of the NWRP. A credit union that falls to a lower net worth category because it failed to implement the steps or to meet the quarterly net worth targets in its NWRP may be required to file a new NWRP, § 702.206(a)(3), thereby revoking the then-current NWRP approving future decreases in earnings retention. *See also* 12 CFR 747.2005(b)(3) (civil money penalty for failure to implement NWRP). In contrast, when a credit union *is* implementing the prescribed steps and meeting its net worth targets, there likely would be no reason to discontinue the decreased earnings retention approved in its NWRP.

Because quarterly review is effectively built-in to the NWRP, proposed new subsection (d) exempted credit unions operating under an NWRP from the quarterly review that § 702.201 imposes on ''adequately capitalized'' credit unions. NCUA received no comments on this exemption. Accordingly, the final rule adopts new subsection (d) as proposed.

7. Section 702.204—PCA for ''Critically Undercapitalized'' Credit Unions

a. *''Other corrective action''.* When a credit union becomes ''critically undercapitalized'' (net worth ratio <2%), part 702 gives the NCUA Board 90 days in which to either place the credit union into conservatorship, liquidate it, or impose ''other corrective action * * * to better achieve the purpose of [PCA].'' 12 U.S.C. 1790d(i)(1); § 702.204(c)(1). NCUA so far has interpreted the option to impose ''other corrective action'' (''OCA'') as requiring some further action in addition to complying with the steps prescribed in an approved NWRP for meeting quarterly net worth targets. Some further action would seem appropriate when a credit union either is not complying with its approved NWRP, or is implementing the prescribed action steps but still failing to achieve its quarterly net worth targets. But when a credit union has been both implementing the steps in its NWRP and timely achieving its net worth targets, demanding further action is superfluous, if not punitive. NCUA has found it difficult to fashion OCA that is more than a makeweight in these circumstances.

Congress left it entirely to the NCUA Board to ''take such other action'' in lieu of conservatorship and liquidation ''as the Board determines would better achieve the purpose of [PCA], after documenting why the action would better achieve that purpose.'' 12 U.S.C. 1790d(i)(1)(b). *See also* S. Rep. No. 193, 105th Cong., 2d Sess. 15 (1998). The NCUA Board has determined that the purpose of PCA—building net worth to minimize share insurance losses—is not undermined by declining to impose OCA when it is documented that a credit union already is achieving the purpose of PCA by complying with an approved NWRP and achieving its prescribed net worth targets. In other words, there would be no reason to demand more than complete success from a credit union that, so far, is completely successful in building net worth.

To implement a more flexible approach to imposing OCA in lieu of conservatorship and liquidation, the proposed rule revised subsection (c)(1)(iii) to provide that ''[OCA] may consist, in whole or in part, of complying with the timetable of quarterly steps and meeting quarterly net worth targets prescribed in an approved [NWRP].'' § 702.204 (c)(1)(iii). This would permit, but not require, NCUA to limit OCA to directing a credit union that already is in compliance with its approved NWRP to simply continue to comply, without undertaking any further action beyond what the NWRP already requires. NCUA received two comments; both supported this shift in approach to implementing OCA. Accordingly, the final rule adopts revised subsection (c)(1)(iii) as proposed.

b. *10-day appeal period.* The NCUA Board's authority to decide whether to conserve a ''critically undercapitalized'' credit union, liquidate it, or allow OCA may be delegated only in the case of credit unions having assets of less than $5 million. 12 U.S.C. 1790d(i)(4); § 702.204(c)(4). In such cases, the credit union has a statutory ''right of direct appeal to the NCUA Board of any decision made by delegated authority.'' *Id.* However, neither the Act nor part 741 sets a deadline by which a credit union must appeal a delegated decision to the NCUA Board. The lack of a deadline for exercising the right to appeal delegated decisions to the NCUA Board gives ''critically undercapitalized'' credit unions at least the appearance of an unlimited opportunity to challenge a Regional Director's decision.

To impose similar finality upon the unfolding timetable of decisions that starts when a credit union becomes ''critically undercapitalized,'' the proposed rule revised subsection (c)(4) to set a deadline of ten calendar days in which to appeal a delegated decision. Objecting that 10 days is too few for small credit unions with unsophisticated management, the one commenter who addressed this section advocated a 30-day appeal period instead. However, the final rule adopts the proposed 10-day appeal period for two reasons. First, it parallels the 10-day window that the Act provides for seeking judicial review of any statutory conservatorship or liquidation. 12 U.S.C. 1786(h)(3), 1787(a)(1)(B). Second, a longer appeal period would unreasonably delay the payout of shares to members that must promptly follow a liquidation.

c. *Insolvent FCU.* The NCUA Board generally must liquidate a credit union eventually if it remains ''critically undercapitalized.'' § 702.204(c). Independently of PCA, however, the Act directs that ''[u]pon its finding that a Federal credit union * * * is insolvent, the Board shall close such credit union for liquidation.'' 12 U.S.C. 1787(a)(1)(A). Therefore, in the case of a ''critically undercapitalized'' *federal* credit union that is insolvent (*i.e.*, has a net worth ratio of less than zero), NCUA has the option of an insolvency-based liquidation. To clarify that this option is available, new subsection (d) to § 702.204 provides that ''a 'critically undercapitalized' federal credit union that has a net worth ratio of less than zero percent (0%) may be placed into liquidation on grounds of insolvency pursuant to [§ 1787(a)(1)(A)].''

8. Section 702.205—Consultation With State Officials on Proposed PCA

As explained above in reference to new subsection (c) of § 702.201, a cross-reference in § 702.205(c) misidentified the decision whether to permit a decrease in a FISCU's quarterly earnings retention as a DSA. To correct this error, the final rule deletes the erroneous cross-reference and relocates the ''consult and seek to work cooperatively'' requirement in § 702.201(c).

9. Section 702.206—Net Worth Restoration Plans

a. *Contents of NWRP.* Section 702.206 prescribes the contents of an NWRP that must be submitted for approval by credit unions classified ''undercapitalized'' or lower.[6] Among the items an NWRP must address is how the credit union will comply with MSAs and DSAs. § 702.206(c)(1)(iii). Some credit unions that were *not* subject to a DSA interpreted that requirement as a demand either to consent to a DSA, or to explain prospectively how the credit union *would* comply with DSAs if the NCUA Board were to impose any. The proposed rule revised subsection (c)(1)(iii) to clarify that an NWRP need only address whatever DSAs, if any, the NCUA Board *already* has imposed on the credit union. The one commenter who addressed this revision supported it. The final rule adopts revised subsection (c)(1)(iii) as proposed.

b. *Publication of NWRP.* Publication of an NWRP is not a prerequisite to enforcing its provisions as authorized in 12 CFR 747.2005, but this fact is not expressly stated in § 702.206 itself. The omission has led some to assume that an NWRP, like a ''Letter of Understanding and Agreement,'' must be published in order to subsequently be enforceable. The Act mandates that a ''written agreement or other written statement'' must be published in order for a violation to be enforceable ''unless the Board, in its discretion, determines that publication would be contrary to the public interest.'' 12 U.S.C. 1786(s)(1)(A). To the extent an NWRP qualifies as a ''written agreement or other written statement'' under § 1786(s)(1)(A), the NCUA Board does not intend to publish NWRPs because it has determined that publication would expose the credit union to reputation risk that would be contrary to the public interest. Therefore, the proposed rule added new subsection (i) to § 702.206, clarifying that ''An NWRP need not be published to be enforceable because publication would be contrary to the public interest.'' NCUA received two comments on the clarification and both supported it. Therefore, the final rule adopts new subsection (i) as proposed.

c. *Alternative capital.* The proposed rule did not reference subsection (e), which permits consideration of any ''regulatory capital'' a credit union may have in evaluating an NWRP. Nonetheless, NCUA received three comments urging the adoption of some form of alternative capital not only to be considered in evaluating an NWRP, but also to offset an applicable RBNW requirement. A fourth commenter opposed alternative capital in any form. The final rule does not address these comments because this rulemaking was not intended by the NCUA Board to be a forum for exploring or introducing alternative forms of capital.

10. Section 702.303—PCA for ''Adequately Capitalized'' New Credit Unions

Under the original alternative system of PCA for new credit unions, a credit union that managed to become ''adequately capitalized'' while still new was subject to the same minimum earnings retention that applies to non-new credit unions that are ''adequately capitalized.'' [7] § 702.201(a). In contrast, ''new'' credit unions that stayed classified below ''adequately capitalized'' were not subject to minimum earnings retention; they had to increase net worth only ''by an amount reflected in the credit union's

[6] As noted earlier in this preamble, the comments on the concept of ''safe harbor'' approval of an NWRP are addressed in a separate proposed rule found elsewhere in this volume of the **Federal Register.**

[7] The final rule corrects the wording of § 702.303, which inadvertently extended that section to ''new'' credit unions classified lower than ''adequately capitalized.'' Sections 702.304 and 702.305 continue to prescribe PCA for new credit unions in those net worth categories.

approved initial or revised business plan.'' § 702.304(a)(1). This created a disincentive for a ''new'' credit union to become ''adequately capitalized'' because the reward for keeping its net worth ratio below 6 percent is that it is relieved from complying with a minimum earnings retention amount.

To eliminate the disincentive, the proposed rule put all new credit unions having a net worth lower than 7 percent in parity for purposes of earnings retention. 67 FR at 38437. An ''adequately capitalized'' new credit union would no longer be subject to the same minimum earnings retention as a non-new counterpart. Instead, like new credit unions in lower categories, it would be required to increase net worth quarterly by ''an amount reflected in its approved initial or revised business plan'' until it becomes ''well capitalized.'' In the absence of such a plan, however, the credit union would remain subject to the same quarterly minimum earnings retention as non-''new'' credit unions.

Two commenters supported parity among new credit unions for earnings retention purposes. Advocating a far less flexible approach, a third commenter (a banking industry trade association) objected that exempting any new credit unions from the statutory minimum earnings retention is not in accordance with CUMAA. That commenter overlooks the fact that CUMAA applies a minimum earnings retention requirement to non-new credit unions; it prescribed no earnings retention requirement at all for new credit unions. 12 U.S.C. 1790d(e)(1). Instead, CUMAA gave NCUA discretion in developing an alternative system of PCA, provided that it recognized that new credit unions initially have no net worth; need reasonable time to accumulate net worth; and need incentives to become ''adequately capitalized'' by the time they no longer qualify as ''new.'' 12 U.S.C. 1790d(b)(2)(B). *See* 64 FR 27090, 27098 (May 18, 1999) (justification for flexible approach). It is entirely consistent with this last statutory criterion to eliminate any disincentive—such as *minimum* earnings retention—for a new credit union to reach ''adequately capitalized'' while it is still ''new.''

11. *Section 702.304—PCA for ''Moderately Capitalized,'' ''Marginally Capitalized'' and ''Minimally Capitalized'' New Credit Unions*

As explained above, the final rule modifies § 702.201(a) to specify that earnings retention must increase the ''the dollar amount'' of net worth, not simply the net worth ratio itself. To conform to that modification, § 702.304(a)(1) is revised accordingly.

12. Section 702.305—PCA for ''Uncapitalized'' New Credit Unions

a. *Member business loan restriction.* Part 702 originally gave an ''uncapitalized'' new credit union full relief from all MSAs while it was operating within the period allowed by its initial business plan to have no net worth. § 702.305(a). An unintended consequence of this forbearance was that ''uncapitalized'' credit unions were free of the MSA restricting MBLs; that restriction applied only when a credit union managed to attain *some* net worth and rise to the ''minimally capitalized'' net worth category.[8] Yet a ''minimally capitalized'' credit union arguably is better suited to expand its MBL portfolio than one that remains ''uncapitalized.'' Further, making PCA *more* demanding as a credit union's net worth and category classification improve, rather than relaxing it, is contrary to the purpose of PCA. To rectify this unintended consequence, the proposed rule extended subsection (a) to include an ''uncapitalized'' new credit union that is operating with no net worth as permitted by an initial business plan. 67 FR at 38437. As a result, ''uncapitalized'' new credit unions are all subjected to the MBL restriction, § 702.305(a)(3), regardless whether they are operating with no net worth under an initial business plan, or have declined to ''uncapitalized'' after reaching a higher net worth category. NCUA received no comments on this section. Accordingly, the final rule adopts revised subsection (a) as proposed.

b. *Filing of revised business plan.* Subsection (a)(2) generally required an ''uncapitalized'' new credit union to submit a revised business plan (''RBP'') within 90 days following either of two events—expiration of the period that the credit union's initial business plan allows it to operate with no net worth, or the effective date that it declined to ''uncapitalized'' from a higher net worth category. This contrasts with the 30-day period that ''moderately capitalized,'' ''marginally capitalized'' and ''minimally capitalized'' credit unions are given to file an RBP. § 702.306(a)(1). Ninety days is an unduly long filing period given that an ''uncapitalized'' credit union faces mandatory conservatorship or liquidation if it fails to increase net worth to at least two percent. Furthermore, it is counterintuitive to give a credit union that *has* a net worth deficit three times as long to devise a plan for generating positive earnings than is given to credit unions that already have net worth.

The proposed rule put all new credit unions that must file an RBP in parity. First, it deleted the 90-day filing window for ''uncapitalized'' credit unions, thereby limiting them to the general 30-day window, once they are required to file an RBP. 67 FR at 38438. Second, it reorganized subsection (a)(2) to parallel the conditions that trigger other less than ''adequately capitalized'' new credit unions to revise their business plans, § 702.304(a)(2), even though only ''uncapitalized'' credit unions are initially allowed to operate with no net worth. To that end, the proposed rule required an ''uncapitalized'' credit union to submit an RBP if it either: fails to increase net worth (*i.e.*, reduce its earnings deficit) as its existing business plan provides; has no approved business plan; or has violated the MSA restricting MBLs.

The sole commenter on this topic supported the 30-day window for filing an RBP, while also urging NCUA to relieve the burden on new credit unions by providing assistance in preparing RBPs. *See* § 702.307(a) (assistance in preparing RBPs). For the reasons set forth above in this section, the revisions to subsection (a)(2) are adopted as proposed.

c. *Liquidation or conservatorship if ''uncapitalized'' after 120 days.* Subsection (c)(2) generally required the NCUA Board to conserve or liquidate an ''uncapitalized'' new credit union that remains ''uncapitalized'' 90 days after its RBP is approved. It was silent, however, regarding conservatorship or liquidation of a credit union whose RBP is rejected. To correct this oversight, the proposed rule mandated conservatorship or liquidation of an ''uncapitalized'' new credit union after a 120-day period regardless whether an RBP has been approved or rejected. 67 FR at 38438. This period combines the 30-day window for submitting an RBP, § 702.306(a)(1), and the original 90-day period allowed for the credit union to develop sufficient positive earnings to avoid conservatorship and liquidation. The 120-day period runs from the later of either the effective date of classification as ''uncapitalized'' or, if a credit union is operating with no net worth in the period prescribed by its initial business plan, the last day of the calendar month after expiration of that period. Because the period for operating with no net worth typically runs on a quarterly basis, the last day of the

[8] The earnings retention requirement, § 702.305(a)(1), is ineffective against an ''uncapitalized'' credit union because a credit union that *has* an undivided earnings deficit has no net worth to retain.

calendar month after it expires parallels the calendar month that separates the quarter-end and the effective date of classification as ''undercapitalized.''

NCUA received no comments on the revisions to subsection (c)(2) and, therefore, they are adopted as proposed. In addition, the final rule relocates to a new subsection (c)(3) the existing exception to mandatory conservatorship or liquidation for a credit union that is able to demonstrate that it is viable and has a reasonable prospect of becoming ''adequately capitalized.''

d. *''Uncapitalized'' new FCU.* As explained above in reference to new subsection (d) of § 702.204, there are two options for liquidating a federal credit union that has no net worth—a PCA-based liquidation, 12 U.S.C. 1787(a)(3)(A)(ii), or an insolvency-based liquidation. 12 U.S.C. 1787(a)(1)(A). Both are available when a new *federal* credit union either fails to timely submit an RBP, § 702.305(c)(1), or remains ''uncapitalized'' 120 days after the effective date of classification, § 702.305(c)(2). To clarify that this option is available, the final rule adds new subsection (d) to § 702.305, providing that ''an 'uncapitalized' federal credit union may be placed into liquidation on grounds of insolvency pursuant to [§ 1787(a)(1)(A)].''

13. Section 702.306—Revised Business Plans for New Credit Unions

a. *Filing schedule.* Subsection (a)(1) required ''moderately capitalized,'' ''marginally capitalized'' and ''minimally capitalized'' credit unions to file an RBP within 30 days after failing to meet a quarterly net worth target prescribed in an existing business plan. As discussed above, the final rule eliminates the 90-day filing window for ''uncapitalized'' credit unions. § 702.305(a)(2). To conform to that modification, the final rule also modifies subsection (a)(1) to apply the 30-day filing window uniformly to all new credit unions classified less than ''adequately capitalized'' or that have violated the MSA restricting MBLs. §§ 702.304(a)(3), 702.305(a)(3).

The original rule's 30-day filing period ran from ''the effective date (per § 702.101(b)) of the credit union's failure to meet a quarterly net worth target prescribed in its then-present business plan.'' § 702.306(a)(1). Even as revised, however, § 702.101(b), which addresses the effective date of classification among the net worth categories, says nothing to determine when a quarterly net worth target is met. The subtlety of this distinction may confuse credit unions that have no then-present approved business plan or have violated the MSA restricting MBLs. Therefore, the proposed rule further revised subsection (a)(1) to effectively give new credit unions that fail to meet a quarterly target 60 days following the quarter-end to file an RBP. § 702.306(a)(1)(i). The 60-day period combines the calendar month that separates the quarter-end from the effective date of classification, with the uniform 30-day filing period that commences on the effective date. Finally, the proposed rule revised subsection (a)(1) still further to clarify that, for new credit unions that either have no approved business plan or that have violated the MBL restriction, the effective date of classification as less than ''adequately capitalized'' triggers the 30-day window for filing an RBP. § 702.306(a)(1)(ii)–(iii). NCUA received no comments on the revisions to the filing schedule for RBPs. Accordingly, revised subsection (a)(1) is adopted as proposed.

b. *Timetable of net worth targets.* Subsection (b)(2) prescribed the contents of an RBP, which must include a timetable of quarterly net worth targets extending for the term of the plan ''so that the credit union becomes 'adequately capitalized' and remains so for four consecutive quarters.'' It also warned that a ''complex'' new credit union that is subject to an RBNW requirement may need to attain a net worth ratio higher than 6 percent to become ''adequately capitalized.'' The proposed rule rectified two flaws in this section. First, in contrast to an NWRP, the objective of an RBP is to build net worth so that a new credit union becomes ''adequately capitalized'' by the time it no longer is ''new,'' [9] rather than by the end of the term of the plan. 65 FR at 8578; 64 FR 27090, 27099 (May 18, 1999) (chart). The proposed rule revised subsection (b)(2) so that an RBP's net worth targets ensure the new credit union will become ''adequately capitalized'' by the time it no longer qualifies as ''new.'' 67 FR at 38438. Second, under part 702 new credit unions cannot be ''complex'' or subject to an RBNW requirement because, by definition, they do not meet the $10 million asset minimum. § 702.103(a)(1). Therefore, the proposed rule deleted the warning to new credit unions that are ''complex.'' NCUA received no comments on either of these revisions. Accordingly, revised subsection (b)(2) is adopted as proposed.

c. *Publication of RBP.* As explained above, the final rule adds a new subsection (i) to § 702.206, to clarify that publication of an NWRP is not a prerequisite to enforcing its provisions as authorized in 12 CFR 747.2005. The same is true of an RBP, but this fact was similarly omitted from § 702.306. To the extent an RBP qualifies as a ''written agreement or other written statement'' under 12 U.S.C. 1786(s)(1)(A), the NCUA Board does not intend to publish RBPs because it has determined that publication would expose the credit union to reputation risk that would be contrary to the public interest. Therefore, the final rule adds new subsection (h) to § 702.306, clarifying that ''An RBP need not be published to be enforceable because publication would be contrary to the public interest.''

13. Section 702.401—Charges to Regular Reserve

a. *Regular reserve.* Although the proposed rule did not reference subsection (b), which requires credit unions ''to establish and maintain a regular reserve account,'' four commenters criticized it as obsolete. The NCUA Board prefers to retain the regular reserve at this time primarily for two reasons. First, it facilitates the statutory earnings retention requirement, 12 U.S.C. 1790d(e), by holding the earnings that credit unions classified ''adequately capitalized'' or lower are required to ''set aside.'' § 702.201. And second, it continues to function as an early warning signal of safety and soundness problems because, as explained below, regulatory review and approval is required before a credit union can take certain actions—charging losses to, and paying dividends from, the regular reserve—that would cause its net worth to decline below 6 percent.

b. *Minimum net worth to charge losses without approval.* Subsection (c)(1) originally allowed the board of directors of a federally-insured credit union that had depleted the balance of its undivided earnings and other reserves to charge losses to the regular reserve account without regulatory approval so long as the charge did not reduce the credit union's net worth classification below ''well capitalized'' (*i.e.*, net worth ratio of 7 percent or greater). § 702.401(c)(1). That net worth category was established as the minimum for charging losses without regulatory approval because the categories below ''well capitalized'' trigger MSAs. However, the proposed rule lowered the minimum category to ''adequately capitalized'' (*i.e.*, 6 percent net worth ratio) in order to give credit unions the flexibility to decide for

[9] A credit union remains ''new'' as long as it is in operation less than 10 years and has assets of $10 million or less. 12 U.S.C. 1790d(o)(4); § 702.301(b).

themselves whether charging losses is worth triggering the single MSA that applies to that category—the quarterly earnings retention. § 702.201(a); 67 FR at 38439. In addition, the proposed rule expressly reminded credit unions that they must deplete their undivided earnings balance before making any charge to the regular reserve. All seven of the commenters who addressed these proposed revisions supported them. Thus, revised subsection (c)(1) is adopted as proposed.

c. *Dual approval to charge losses.* Subsection (c)(2) originally required the prior approval of the ''appropriate State official,'' but not the approval of the ''appropriate Regional Director,'' when a State-chartered credit union seeks to charge losses that would cause it to decline below the minimum category. Omitting the approval of NCUA Regional Directors was inconsistent with the protocol applied elsewhere in part 702 requiring joint State and Federal approval of PCA decisions affecting State-chartered credit unions. *E.g.,* §§ 702.206(a)(1), 702.306(a)(1). To correct this inconsistency, the proposed rule modified § 702.401(c)(2) to require the concurrence of both the ''appropriate State official'' *and* ''the appropriate Regional Director'' to permit a State-chartered credit union to charge losses to the regular reserve. In addition, the proposed rule clarified that written approval may consist of an approved NWRP that allows such charges.

The sole commenter on the revisions proposed for subsection (c)(2) objected that the dual approval requirement would unnecessarily overburden NCUA with the oversight of State officials. On the contrary, the NCUA Board does not consider its approval to be a function of overseeing State officials. Rather, its approval for a State-chartered credit union to charge losses to the regular reserve is integral to PCA because of NCUA's independent role as insurer of the shares and deposits of federally-insured State-chartered credit unions. Accordingly, revised subsection (c)(2) is adopted as proposed.

15. Section 702.403—Payment of Dividends

a. *Minimum net worth to pay dividends without approval.* Subsection (b)(1) originally allowed the board of directors of a federally-insured credit union that had depleted the balance of undivided earnings to pay dividends out of the regular reserve account without regulatory approval so long as it did not cause the credit union to decline below ''well capitalized.'' § 702.403(b)(1). As explained above in regard to § 702.401(c)(1), the proposed rule similarly lowered to ''adequately capitalized'' the minimum net worth category in which credit unions may pay dividends out of the regular reserve without regulatory approval. This would give credit unions that have depleted undivided earnings the flexibility to decide for themselves whether drawing down the regular reserve to pay dividends is worth triggering the quarterly earnings retention requirement that applies to ''adequately capitalized'' credit unions. § 702.201(a).

b. *Dual approval to pay dividends.* As with § 702.401(c)(2) discussed above, subsection (b)(2) originally required the prior approval of the ''appropriate State official,'' but not the approval of the ''appropriate Regional Director,'' when paying dividends out of the regular reserve would cause a State-chartered credit union to decline below the minimum net worth category. In addition, omitting Regional Director approval may suggest, incorrectly, that a State official's approval to pay dividends from the regular reserve under § 702.401(b) makes it unnecessary to independently obtain both the State official's and the Regional Director's approval under § 702.201(b) for a State-chartered credit union to decrease its earnings retention in order to pay dividends. For this reason and the reason explained in the preceding section, the proposed rule corrected this omission by revising subsection (b)(2) to require the concurrence of both the ''appropriate State official'' *and* ''the appropriate Regional Director'' for a State-chartered credit union to pay dividends out of its regular reserve. In addition, the proposed rule clarified that written approval may consist of an approved NWRP that allows such dividend payments. The two commenters who addressed the revisions proposed for subsections (b)(1) and (b)(2) supported them. Accordingly, they are adopted as proposed.

Subpart A of Part 741—Requirements for Insurance

16. Section 741.3—Adequacy of Reserves

Subsection (a)(2) originally allowed State-chartered credit unions to charge losses other than loan losses to the regular reserve in accordance with State law or procedures, but without regulatory approval, provided that the charges did not cause the credit union to decline below ''well capitalized.'' 12 CFR 741.3(a)(2). The preceding subsection (a)(1) incorporates by reference all of part 702 as a prerequisite for insurability of State-chartered credit unions. As discussed above, § 702.401(c) already imposes on State-chartered credit unions the same conditions for regulatory approval that subsection (a)(2) prescribes for an insured credit union seeking to charge losses to the regular reserve. Because this makes subsection (a)(2) redundant, the final rule eliminates it from § 741.3.

The final rule's removal of subsection (a)(2) does not mean that § 702.401(c) preempts ''either state law or procedures established by the appropriate State official'' that restrict a State-chartered credit union's ability to charge losses to the regular reserve. On the contrary, such charges would independently remain subject to applicable State laws and procedures. Further, an appropriate State official would retain complete discretion to withhold approval of such charges, under § 702.401(c)(2), on grounds that they would violate State law or procedures.

Subpart L of Part 747—Issuance, Review and Enforcement of Orders Imposing PCA

17. Section 747.2005—Enforcement of Orders

The NCUA Board is authorized to ''assess a civil money penalty against a credit union which fails to implement a net worth restoration plan * * * or a revised business plan under * * * part 702.'' 12 CFR 747.2005(b)(2). As explained above, the NCUA Board has determined that it is not in the public interest to require publication of an NWRP or an RBP in order for either to be enforceable and §§ 702.206 and 702.306 are modified accordingly. The final rule makes a conforming modification to § 747.2005(b)(2) to provide that a civil money penalty may be assessed for failure to implement a plan ''regardless whether the plan was published.''

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis describing any significant economic impact a proposed regulation may have on a substantial number of small credit unions (primarily those under $1 million in assets). The proposed rule improves and simplifies the existing system of PCA mandated by Congress. 12 U.S.C. 1790d. The NCUA Board has determined and certifies that the final rule will not have a significant economic impact on a substantial number of small credit unions and, therefore, a Regulatory Flexibility Analysis is not required.

Paperwork Reduction Act

The reporting requirements in this final rule have been submitted to the Office of Management and Budget. Under the Paperwork Reduction Act of 1995, no person is required to respond to a collection of information unless it displays a valid OMB number. Control number 3133–0161 has been issued for part 702 and will be displayed in the table at 12 CFR part 795.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their regulatory actions on State and local interests. NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily adheres to the fundamental federalism principles addressed by the executive order. This final rule will apply to all federally-insured credit unions, including State-chartered credit unions. Accordingly, it may have a direct effect on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government. This impact is an unavoidable consequence of carrying out the statutory mandate to adopt a system of prompt corrective action to apply to all federally-insured credit unions. NCUA staff has consulted with a committee of representative State regulators regarding the impact of the proposed revisions on State-chartered credit unions. Their comments and suggestions are reflected in the proposed rule.

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by section 551 of the Administrative Procedure Act, 5 U.S.C. 551. The Office of Management and Budget has determined that this rule is not a major rule.

List of Subjects

12 CFR Parts 702 and 741

Credit unions, Reporting and recordkeeping requirements.

12 CFR Part 747

Administrative practices and procedures, Credit unions.

By the National Credit Union Administration Board on November 21, 2002.

Becky Baker,

Secretary of the Board.

For the reasons set forth above, 12 CFR parts 702, 741 and 747 are amended as follows:

PART 702—PROMPT CORRECTIVE ACTION

1. The authority citation for part 702 continues to read as follows:

Authority: 12 U.S.C. 1766(a), 1790d.

2. Amend § 702.2 as follows:

a. Redesignate current paragraphs (i) through (k) as new paragraphs (j) through (l) respectively.

b. Add new paragraph (i) to read as set forth below;

c. Revise newly designated paragraph (k)(1)(i) to read as set forth below;

d. Revise newly designated paragraph (k)(1)(iv) to read as set forth below; and

e. Remove from newly designated paragraph (k)(2) the cross-reference to ''paragraph (j)(1)'' and add in its place a cross-reference to ''paragraph (k)(1)''.

§ 702.2 Definitions.

* * * * *

(i) *Senior executive officer* means a senior executive officer as defined by 12 CFR 701.14(b)(2).

* * * * *

(k) *Total assets.* (1) * * *

(i) *Average quarterly balance.* The average of quarter-end balances of the current and three preceding calendar quarters; or

* * *

(iv) *Quarter-end balance.* The quarter-end balance of the calendar quarter as reported on the credit union's Call Report.

* * * * *

3. Amend § 702.101 as follows:

a. Add a heading to paragraph (b)(1) to read as set forth below;

b. Revise paragraph (b)(2) to read as set forth below;

c. Add a heading to paragraph (b)(3) to read as set forth below; and

d. Revise the heading of paragraph (c), and paragraph (c)(1), to read as follows:

§ 702.101 Measures and effective date of net worth classification.

* * * * *

(b) * * *

(1) *Quarter-end effective date.* * * *

(2) *Corrected net worth category.* The date the credit union received subsequent written notice from NCUA or, if State-chartered, from the appropriate State official, of a decline in net worth category due to correction of an error or misstatement in the credit union's most recent Call Report; or

(3) *Reclassification to lower category.* * * *

(c) *Notice to NCUA by filing Call Report.* (1) Other than by filing a Call Report, a federally-insured credit union need not notify the NCUA Board of a change in its net worth ratio that places the credit union in a lower net worth category;

* * * * *

4. Amend § 702.102 by revising Table 1 immediately preceding paragraph (b) to read as follows:

§ 702.102 Statutory net worth categories.

* * * * *

TABLE 1 – STATUTORY NET WORTH CATEGORY CLASSIFICATION

A credit union's net worth category is . . .	*if its net worth ratio is . . .*	*and subject to the following condition(s) . . .*
"Well Capitalized"	7% or above	Meets applicable risk-based net worth (RBNW) requirement
"Adequately Capitalized"	6% to 6.99%	Meets applicable RBNW requirement
"Undercapitalized"	4% to 5.99%	Or fails applicable RBNW requirement
"Significantly Undercapitalized"	2% to 3.99%	Or if "undercapitalized" at <5% net worth ratio and fails to timely submit or materially implement Net Worth Restoration Plan
"Critically Undercapitalized"	Less than 2%	None

* * * * *

§ 702.103 [Amended]

5. Amend § 702.103 as follows:

a. Remove the heading from paragraph (a);

b. Remove paragraph (b); and

c. Redesignate current paragraph (a) as the sectional introductory text, and paragraphs (a)(1) and (a)(2) as paragraphs (a) and (b), respectively.

§ 702.104 [Amended]

6. Amend § 702.104 as follows:

a. Remove the number ''1'' from the parenthetical ''(Table 1)'' in the introductory text and add in its place the number ''2''; and

b. Redesignate Table 1 immediately following paragraph (h) as Table 2.

§ 702.105 [Amended]

7. Amend § 702.105 as follows:

a. Remove the number ''2'' from the parenthetical ''(Table 2)'' in the introductory text and add in its place the number ''3'';

b. Remove the citation ''§ 702.2(k)'' in the introductory text and add in its place the citation ''§ 702.2(m)''; and

c. Redesignate Table 2 immediately following paragraph (b) as Table 3.

§ 702.106 [Amended]

8. Amend § 702.106 as follows:

a. Remove the number ''3'' from the parenthetical ''(Table 3)'' in the introductory text and add in its place the number ''4''; and

b. Redesignate Table 3 immediately following paragraph (h) as Table 4.

9. Amend § 702.107 as follows:

a. Remove the number ''4'' from the parenthetical ''(Table 4)'' in the introductory text and adding in its place the number ''5'';

b. Revise paragraph (a) to read as set forth below;

c. Add new paragraph (d) immediately after paragraph (c)(6) to read as set forth below;

d. Redesignate Table 4 immediately following new paragraph (d) as Table 5;

e. Revise section (a) to Table 5 to read as set forth below; and

f. Add new section (d) to Table 5 as follows:

§ 702.107 Alternative components for standard calculation.

* * * * *

(a) *Long-term real estate loans.* The sum of:

(1) *Non-callable.* Non-callable long-term real estate loans as follows:

(i) Eight percent (8%) of the amount of such loans with a remaining maturity of greater than 5 years, but less than or equal to 12 years;

(ii) Twelve percent (12%) of the amount of such loans with a remaining maturity of greater than 12 years, but less than or equal to 20 years; and

(iii) Fourteen percent (14%) of the amount of such loans with a remaining maturity greater than 20 years;

(2) *Callable.* Long-term real estate loans callable in 5 years or less as follows:

(i) Six percent (6%) of the amount of such loans with a documented call provision of 5 years or less and with a remaining maturity of greater than 5 years, but less than or equal to 12 years;

(ii) Ten percent (10%) of the amount of such loans with a documented call provision of 5 years or less and with a remaining maturity of greater than 12 years, but less than or equal to 20 years; and

(iii) Twelve percent (12%) of the amount of such loans with a documented call provision of 5 years or less and with a remaining maturity of greater than 20 years;

* * * * *

(d) *Loans sold with recourse.* The alternative component is the sum of:

(1) Six percent (6%) of the amount of loans sold with contractual recourse obligations of six percent (6%) or greater; and

(2) The weighted average recourse percent of the amount of loans sold with contractual recourse obligations of less than six percent (6%), as computed by the credit union.

(a) LONG-TERM REAL ESTATE LOANS

Amount of long-term real estate loans by remaining maturity	*Alternative risk weighting*
Non-callable long-term real estate loans	
Remaining maturity:	
> 5 years to 12 years	.08
> 12 years to 20 years	.12
> 20 years	.14
Long-term real estate loans callable in 5 years or less	
Remaining maturity:	
> 5 years to 12 years	.06
> 12 years to 20 years	.10
> 20 years	.12
The "alternative component" is the sum of each amount of the "long-term real estate loans" risk portfolio by non-"callable" and "callable" characteristic and by remaining maturity (as a percent of quarter-end total assets) times its alternative factor. Substitute for corresponding standard component if smaller.	

* * * * * * *

(d) LOANS SOLD WITH RECOURSE

Amount of loans by recourse	*Alternative risk weighting*
Recourse 6% or greater	.06
Recourse <6%	Weighted average recourse percent
The "alternative component" is the sum of each amount of the "loans sold with recourse" risk portfolio by level of recourse (as a percent of quarter-end total assets) times its alternative factor. The alternative factor for loans sold with recourse of less than 6% is equal to the weighted average recourse percent on such loans. A credit union must compute the weighted average recourse percent for its loans sold with recourse of less than six percent (6%). Substitute for corresponding standard component if smaller.	

10. Amend § 702.108 as follows:

a. Revise the section heading to read as set forth below;

b. Redesignate current paragraphs (a) and (b) as paragraphs (b) and (c), respectively;

c. Add a new paragraph (a) as set forth below; and

d. Revise newly designated paragraph (b) to read as set forth below.

§ 702.108 Risk mitigation credit.

(a) *Who may apply.* A credit union may apply for a risk mitigation credit if on any of the current or three preceding effective dates of classification it either failed an applicable RBNW requirement or met it by less than 100 basis points.

(b) *Application for credit.* Upon application pursuant to guidelines duly adopted by the NCUA Board, the NCUA Board may in its discretion grant a credit to reduce a risk-based net worth requirement under §§ 702.106 and 702.107 upon proof of mitigation of:

(1) Credit risk; or

(2) Interest rate risk as demonstrated by economic value exposure measures.

* * * * *

11. Revise the heading of Appendixes A–F to Subpart A of Part 702 to read as follows:

Appendixes A–H to Subpart A of Part 702

12. Revise Appendix C to Subpart A to read as follows:

APPENDIX C – EXAMPLE LONG-TERM REAL ESTATE LOANS
ALTERNATIVE COMPONENT, §702.107(a)
(EXAMPLE CALCUATION IN BOLD)

Remaining maturity	**Dollar balance of Long-term real estate loans by remaining maturity**	**Percent of total assets by remaining maturity**	Alternative risk weighting	**Alternative component**
Non-callable long-term real estate loans				
> 5 years to 12 years	**15,000,000**	**7.5000 %**	.08	**0.6000 %**
> 12 years to 20 years	**2,500,000**	**1.2500 %**	.12	**0.1500 %**
> 20 years	**2,500,000**	**1.2500 %**	.14	**0.1750 %**
Long-term real estate loans callable in 5 years or less				
> 5 years to 12 years	**35,000,000**	**17.5000 %**	.06	**1.0500 %**
> 12 years to 20 years	**5,000,000**	**2.5000 %**	.10	**0.2500 %**
> 20 years	**0**	**0.000 %**	.12	**0.000 %**
Sum of above equals Alternative Component*				**2.23 %**

*Substitute for standard component if lower.

13. Redesignate Appendix F to Subpart A as Appendix H.

14. Add new Appendixes F and G to Subpart A to read as follows:

APPENDIX F – EXAMPLE LOANS SOLD WITH RECOURSE
ALTERNATIVE COMPONENT, §702.107(d)
(EXAMPLE CALCULATION IN BOLD)

Percent of contractual recourse obligation	***Dollar balance of Loans sold with recourse***	***Percent of total assets***	***Alternative risk weighting***	***Alternative component***
Recourse 6 % or greater	**5,000,000**	**2.5000 %**	.06	**0.1500 %**
Recourse < 6 %	**35,000,000**	**17.5000 %**	.0500 [a/]	**0.8750 %**
Sum of above equals Alternative component*				**1.03 %**

* Substitute for corresponding standard component if lower.

[a/] The credit union must calculate this alternative risk weighting for loans sold with recourse of less than 6 %. For an example computation, see worksheet in Appendix G below.

APPENDIX G –WORKSHEET FOR ALTERNATIVE RISK WEIGHTING OF LOANS SOLD WITH CONTRACTUAL RECOURSE OBLIGATIONS OF LESS THAN 6 %
(EXAMPLE CALCULATION IN BOLD)

Percent of contractual recourse obligation less than 6%	*Dollar balance of loans sold with recourse*	*Dollars of recourse*	*Alternative risk weighting*
5.50 %	5,000,000	275,000	
5.00 %	25,000,000	1,250,000	
4.50 %	5,000,000	225,000	
Sum of above equals	35,000,000	1,750,000	
Dollar of recourse divided by dollar balance equals (expressed as %)			5.00 %

15. Revise newly designated Appendix H to Subpart A to read as follows:

APPENDIX H -- EXAMPLE RBNW REQUIREMENT USING ALTERNATIVE COMPONENTS
(EXAMPLE CALCULATION IN BOLD)

Risk portfolio	*Standard component*	*Alternative component*	*Lower of standard or alternative component*
(a) Long-term real estate loans	2.20 %	2.85 %	2.20 %
(b) MBLs outstanding	0.77 %	0.95 %	0.77 %
(c) Investments	1.51 %	1.37 %	1.37 %
(f) Loans sold with recourse	1.20%	1.03%	1.03%
			Standard component
(d) Low-risk assets			0 %
(e) Average-risk assets			1.83 %
(g) Unused MBL commitments			0.15 %
(h) Allowance			(1.02) %
RBNW requirement* Compare to Net Worth Ratio			6.33 %

* A credit union is "undercapitalized" if its net worth ratio is less than its applicable RBNW requirement.

16. Revise § 702.201 to read as follows:

§ 702.201 Prompt corrective action for ''adequately capitalized'' credit unions.

(a) *Earnings retention.* Beginning the effective date of classification as ''adequately capitalized'' or lower, a federally-insured credit union must increase the dollar amount of its net worth quarterly either in the current quarter, or on average over the current and three preceding quarters, by an amount equivalent to at least 1/10th percent (0.1%) of its total assets, and must quarterly transfer that amount (or more by choice) from undivided earnings to its regular reserve account until it is ''well capitalized.''

(b) *Decrease in retention.* Upon written application received no later than 14 days before the quarter end, the NCUA Board, on a case-by-case basis, may permit a credit union to increase the dollar amount of its net worth and quarterly transfer an amount that is less than the amount required under paragraph (a) of this section, to the extent the NCUA Board determines that such lesser amount—

(1) Is necessary to avoid a significant redemption of shares; and

(2) Would further the purpose of this part.

(c) *Decrease by FISCU.* The NCUA Board shall consult and seek to work cooperatively with the appropriate State official before permitting a federally-insured State-chartered credit union to decrease its earnings retention under paragraph (b) of this section.

(d) *Periodic review.* A decision under paragraph (b) of this section to permit a credit union to decrease its earnings retention is subject to quarterly review and revocation except when the credit union is operating under an approved net worth restoration plan that provides for decreasing its earnings retention as provided under paragraph (b).

§ 702.202 [Amended]

17. Amend § 702.202 as follows:

a. Remove the word ''transfer'' from the heading of paragraph (a)(1) and add in its place the word ''retention.''

b. Remove the words ''or interest'' from the heading and from the text of paragraph (b)(3).

§ 702.203 [Amended]

18. Amend § 702.203 as follows:

a. Remove the word ''transfer'' from the heading of paragraph (a)(1) and add in its place the word ''retention.''

b. Remove the words ''or interest'' from the heading and from the text of paragraph (b)(3).

19. Amend § 702.204 as follows:

a. Revise the heading of paragraph (a)(1) to read as set forth below;

b. Revise paragraph (b)(3) to read as set forth below;

c. Revise paragraph (c)(1)(iii) to read as set forth below;

d. Revise paragraph (c)(4) to read as set forth below; and

e. Add new paragraph (d) to read as follows:

§ 702.204 Prompt corrective action for ''critically undercapitalized'' credit unions.

(a) * * *

(1) *Earnings retention.* * * *

* * * * *

(b) * * *

(3) *Restricting dividends paid.* Restrict the dividend rates that the credit union pays on shares as provided in § 702.202(b)(3).

* * * * *

(c) * * *

(1) * * *

(iii) *Other corrective action.* Take other corrective action, in lieu of conservatorship or liquidation, to better achieve the purpose of this part, provided that the NCUA Board documents why such action in lieu of conservatorship or liquidation would do so, *provided however,* that other corrective action may consist, in whole or in part, of complying with the quarterly timetable of steps and meeting the quarterly net worth targets prescribed in an approved net worth restoration plan.

* * *

(4) *Nondelegation.* The NCUA Board may not delegate its authority under paragraph (c) of this section, unless the credit union has less than $5,000,000 in total assets. A credit union shall have a right of direct appeal to the NCUA Board of any decision made by delegated authority under this section within ten (10) calendar days of the date of that decision.

(d) *Mandatory liquidation of insolvent federal credit union.* In lieu of paragraph (c) of this section, a ''critically undercapitalized'' federal credit union that has a net worth ratio of less than zero percent (0%) may be placed into liquidation on grounds of insolvency pursuant to 12 U.S.C. 1787(a)(1)(A).

§ 702.205 [Amended]

20. Amend § 702.205 as follows:

a. Remove from paragraph (a)(1) the words ''place the credit union into conservatorship or liquidation'' and add in their place the words ''take the proposed action''; and

b. Remove from paragraph (c) the citation ''702.201(b)''.

21. Amend § 702.206 as follows:

a. Revise paragraph (c)(1)(ii) to read as set forth below;

b. Revise paragraph (c)(1)(iii) to read as set forth below; and

c. Add new paragraph (i) to read as follows:

§ 702.206 Net worth restoration plans.

* * * * *

(c) * * *

(1) * * *

(ii) The projected amount of earnings to be transferred to the regular reserve account in each quarter of the term of the NWRP as required under § 702.201(a), or as permitted under § 702.201(b);

(iii) How the credit union will comply with the mandatory and any discretionary supervisory actions imposed on it by the NCUA Board under this subpart;

* * * * *

(i) *Publication.* An NWRP need not be published to be enforceable because publication would be contrary to the public interest.

22. Amend § 702.302 as follows:

a. Remove the number ''2'' from the parenthetical ''(Table 2)'' in the introductory text of paragraph (c) and add in its place the number ''6'';

b. Revise the table immediately preceding paragraph (d) to read as set forth below; and

c. Revise paragraph (d) to read as follows:

§ 702.302 Networth categories for new credit unions.

* * * * *

TABLE 6 -- NET WORTH CATEGORY CLASSIFICATION FOR "NEW" CREDIT UNIONS

A "new" credit union's net worth category is . . .	*if its net worth ratio is . . .*
"Well Capitalized"	7% or above
"Adequately Capitalized"	6% to 6.99%
"Moderately Capitalized"	3.5% to 5.99%
"Marginally Capitalized"	2% to 3.49%
"Minimally Capitalized"	0% to 1.99%
"Uncapitalized"	Less than 0%

(d) *Reclassification based on supervisory criteria other than net worth.* Subject to § 702.102(b) and (c), the NCUA Board may reclassify a ''well capitalized,'' ''adequately capitalized'' or ''moderately capitalized'' new credit union to the next lower net worth category (each of such actions is hereinafter referred to generally as ''reclassification'') in either of the circumstances prescribed in § 702.102(b).

* * * * *

23. Revise § 702.303 to read as follows:

§ 702.303 Prompt corrective action for ''adequately capitalized'' new credit unions.

Beginning on the effective date of classification, an ''adequately capitalized'' new credit union must increase the dollar amount of its net worth by the amount reflected in its approved initial or revised business plan in accordance with § 702.304(a)(2), or in the absence of such a plan, in accordance with § 702.201, and quarterly transfer that amount from undivided earnings to its regular reserve account, until it is ''well capitalized.''

24. Amend § 702.304 by revising paragraph (a) to read as follows:

§ 702.304 Prompt corrective action for ''moderately capitalized,'' ''marginally capitalized'' and ''minimally capitalized'' new credit unions.

(a) *Mandatory supervisory actions by new credit union.* Beginning on the date of classification as ''moderately capitalized,'' ''marginally capitalized'' or minimally capitalized'' (including by reclassification under § 702.302(d)), a new credit union must—

(1) *Earnings retention.* Increase the dollar amount of its net worth by the amount reflected in its approved initial or revised business plan and quarterly transfer that amount from undivided earnings to its regular reserve account;

(2) *Submit revised business plan.* Submit a revised business plan within the time provided by § 702.306 if the credit union either:

(i) Has not increased its net worth ratio consistent with its then-present approved business plan;

(ii) Has no then-present approved business plan; or

(iii) Has failed to comply with paragraph (a)(3) of this section; and

(3) *Restrict member business loans.* Not increase the total dollar amount of member business loans (defined as loans outstanding and unused commitments to lend) as of the preceding quarter-end unless it is granted an exception under 12 U.S.C. 1757a(b).

* * * * *

25. Amend § 702.305 as follows:

a. Revise paragraph (a) as set forth below;

b. Revise paragraph (c)(2) as set forth below; and

c. Add new paragraphs (c)(3) and (d) as follows:

§ 702.305 Prompt corrective action for ''uncapitalized'' credit unions.

(a) *Mandatory supervisory actions by new credit union.* Beginning on the effective date of classification as ''uncapitalized,'' a new credit union must—

(1) *Earnings retention.* Increase the dollar amount of its net worth by the amount reflected in the credit union's approved initial or revised business plan;

(2) *Submit revised business plan.* Submit a revised business plan within the time provided by § 702.306, providing for alternative means of funding the credit union's earnings deficit, if the credit union either:

(i) Has not increased its net worth ratio consistent with its then-present approved business plan;

(ii) Has no then-present approved business plan; or

(iii) Has failed to comply with paragraph (a)(3) of this section; and

(3) *Restrict member business loans.* Not increase the total dollar amount of member business loans as provided in § 702.304(a)(3).

* * * * *

(c) * * *

(2) *Plan rejected, approved, implemented.* Except as provided in paragraph (c)(3) of this section, must place into liquidation pursuant to 12 U.S.C. 1787(a)(3)(A)(ii), or conservatorship pursuant to 12 U.S.C. 1786(h)(1)(F), an ''uncapitalized'' new credit union that remains ''uncapitalized'' one hundred twenty (120) calendar days after the later of:

(i) The effective date of classification as ''uncapitalized''; or

(ii) The last day of the calendar month following expiration of the time period provided in the credit union's initial business plan (approved at the time its charter was granted) to remain ''uncapitalized,'' regardless whether a revised business plan was rejected, approved or implemented.

(3) *Exception.* The NCUA Board may decline to place a new credit union into liquidation or conservatorship as provided in paragraph (c)(2) of this section if the credit union documents to the NCUA Board why it is viable and has a reasonable prospect of becoming ''adequately capitalized.''

(d) *Mandatory liquidation of ''uncapitalized'' federal credit union.* In lieu of paragraph (c) of this section, an ''uncapitalized'' federal credit union may be placed into liquidation on grounds of insolvency pursuant to 12 U.S.C. 1787(a)(1)(A).

26. Amend § 702.306 as follows:

a. Revise paragraph (a) to read as set forth below;

b. Revise paragraph (b)(2) to read as set forth below; and

c. Add new paragraph (h) to read as follows:

§ 702.306 Revised business plans for new credit unions.

(a) *Schedule for filing.* (1) *Generally.* Except as provided in paragraph (a)(2) of this section, a new credit union classified ''moderately capitalized'' or lower must file a written revised business plan (RBP) with the appropriate Regional Director and, if State-chartered, with the appropriate State official, within 30 calendar days of either:

(i) The last of the calendar month following the end of the calendar quarter that the credit union's net worth ratio has not increased consistent with its the-present approved business plan;

(ii) The effective date of classification as less than ''adequately capitalized'' if the credit union has no then-present approved business plan; or

(iii) The effective date of classification as less than ''adequately capitalized'' if the credit union has increased the total amount of member business loans in violation of § 702.304(a)(3).

(2) *Exception.* The NCUA Board may notify the credit union in writing that its RBP is to be filed within a different period or that it is not necessary to file an RBP.

(3) *Failure to timely file plan.* When a new credit union fails to file an RBP as provided under paragraphs (a)(1) or (a)(2) of this section, the NCUA Board shall promptly notify the credit union that it has failed to file an RBP and that it has 15 calendar days from receipt of that notice within which to do so.

(b) * * *

(2) Establish a timetable of quarterly targets for net worth during each year in which the RBP is in effect so that the credit union becomes ''adequately capitalized'' by the time it no longer qualifies as ''new'' per § 702.301(b);

* * * * *

(h) *Publication.* An RBP need not be published to be enforceable because publication would be contrary to the public interest.

27. Amend § 702.401 by revising paragraph (c) to read as follows:

§ 702.401 Reserves.

* * * * *

(c) *Charges to regular reserve after depleting undivided earnings.* The board of directors of a federally-insured credit union may authorize losses to be charged to the regular reserve after first depleting the balance of the undivided earnings account and other reserves, provided that the authorization states the amount and provides an explanation of the need for the charge, and either—

(1) The charge will not cause the credit union's net worth classification to fall below ''adequately capitalized'' under subparts B or C of this part; or

(2) If the charge will cause the net worth classification to fall below ''adequately capitalized,'' the appropriate Regional Director and, if State-chartered, the appropriate State official, have given written approval (in an NWRP or otherwise) for the charge.

* * * * *

28. Amend § 702.403 by revising paragraph (b) to read as follows:

§ 702.403 Payment of dividends.

* * * * *

(b) *Payment of dividends if undivided earnings depleted.* The board of directors of a ''well capitalized'' federally-insured credit union that has depleted the balance of its undivided earnings account may authorize a transfer of funds from the credit union's regular reserve account to undivided earnings to pay dividends, provided that either—

(1) The payment of dividends will not cause the credit union's net worth classification to fall below ''adequately capitalized'' under subpart B or C of this part; or

(2) If the payment of dividends will cause the net worth classification to fall below ''adequately capitalized,'' the appropriate Regional Director and, if State-chartered, the appropriate State official, have given prior written approval (in an NWRP or otherwise) to pay a dividend.

PART 741—REQUIREMENTS FOR INSURANCE

1. The authority citation for part 741 continues to read as follows:

Authority: 12 U.S.C. 1757, 1766, 1781–1790, and 1790d. Section 741.4 is also authorized by 31 U.S.C. 3717.

§ 741.3. [Amended]

2. Amend § 741.3 as follows:

a. Remove from the heading of paragraph (a) the words ''Adequacy of''.

b. Remove paragraph (a)(2); and

c. Redesignate current paragraph (a)(3) as paragraph (a)(2).

PART 747—ADMINISTRATIVE ACTIONS, ADJUDICATIVE HEARINGS, RULES OF PRACTICE AND PROCEDURE, AND INVESTIGATIONS

1. The authority citation for part 747 continues to read as follows:

Authority: 12 U.S.C. 1766, 1786, 1784, 1787, 1790d and 4806(a); and 42 U.S.C. 4012a.

2. Amend § 747.2005 of subpart L by revising paragraph (b)(2) to read as follows:

§ 747.2005 Enforcement of orders.

* * * * *

(b) * * *

(2) *Failure to implement plan.* Pursuant to 12 U.S.C. 1786(k)(2)(A), the NCUA Board may assess a civil money penalty against a credit union which fails to implement a net worth restoration plan under subpart B of part 702 of this chapter or a revised business plan under subpart C of part 702, regardless whether the plan was published.

* * * * *

[FR Doc. 02–30091 Filed 11–27–02; 8:45 am]

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DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

14 CFR Part 39

[Docket No. 2002–NE–16–AD; Amendment 39–12952; AD 2002–23–08]

RIN 2120–AA64

Airworthiness Directives; Rolls-Royce plc. RB211–535 Turbofan Engines

AGENCY: Federal Aviation Administration, DOT.

ACTION: Final rule; request for comments.

SUMMARY: This amendment adopts a new airworthiness directive (AD) that is applicable to Rolls-Royce plc. (RR) models RB211–535E4–37, RB211–535E4–B–37, and RB211–535E4–B–75 turbofan engines, with certain part number (P/N) low pressure (LP) turbine stage 2 discs installed. This action requires establishing new reduced LP turbine stage 2 disc cyclic limits. This action also requires removing from service affected discs that already exceed the new reduced cyclic limit, and removing other affected discs before exceeding their cyclic limits, using a drawdown schedule. The actions specified in this AD are intended to prevent LP turbine stage 2 disc failure, which could result in uncontained engine failure and possible loss of the airplane.

DATES: Effective December 30, 2002. The incorporation by reference of certain publications listed in the rule is approved by the Director of the Federal Register as of December 30, 2002.

Comments for inclusion in the Rules Docket must be received on or before January 28, 2003.

ADDRESSES: Submit comments in triplicate to the Federal Aviation Administration (FAA), New England Region, Office of the Regional Counsel, Attention: Rules Docket No. 2002–NE–16–AD, 12 New England Executive Park, Burlington, MA 01803–5299. Comments may be inspected at this location, by appointment, between 8 a.m. and 4:30 p.m., Monday through Friday, except Federal holidays. Comments may also be sent via the Internet using the following address: *9-ane-adcomment@faa.gov.* Comments sent via the Internet must contain the docket number in the subject line.

The service information referenced in this AD may be obtained from Rolls-Royce plc, P.O. Box 31 Derby, DE24 8BJ, United Kingdom; telephone 011–44–1332–242424; fax 011–44–1332–249936. This information may be examined, by appointment, at the FAA, New England Region, Office of the Regional Counsel, 12 New England Executive Park, Burlington, MA; or at the Office of the Federal Register, 800 North Capitol Street, NW., Suite 700, Washington, DC.

FOR FURTHER INFORMATION CONTACT: Ian Dargin, Aerospace Engineer, Engine Certification Office, FAA, Engine and Propeller Directorate, 12 New England Executive Park, Burlington, MA 01803–5299; telephone (781) 238–7178; fax (781) 238–7199.

SUPPLEMENTARY INFORMATION: The Civil Aviation Authority (CAA), which is the airworthiness authority for the United Kingdom (U.K.), recently notified the FAA that an unsafe condition may exist on RR models RB211–535E4–37, RB211–535E4–B–37, and RB211–535E4–B–75 turbofan engines. The CAA advises that a reassessment of the safe cyclic limits of LP turbine stage 2 discs, P/N's UL11508, UL17141, UL18947, UL29029, and UL37352 has been performed by the manufacturer. The cyclic limits of these discs are reduced based on more recent thermal and stress data obtained from operational experience. This condition, if not corrected, could result in uncontained engine failure and possible loss of the airplane.

Manufacturer's Service Information

Rolls-Royce plc. has issued mandatory service bulletin (MSB) RB.211–72–D181, Revision 3, dated August 16, 2002, that specifies a drawdown schedule for removing from service affected LP turbine stage 2 discs, using new Time Limits Manual (TLM) cyclic limits. This MSB provides a scheduled reduction, by engine and flight plan, of LP turbine stage 2 disc lives until the full life-cycle reduction on December 31, 2005. This MSB also provides instructions for performing a one-time on-wing eddy current inspection for cracks of affected LP turbine stage 2 discs to allow a disc to remain in service for an additional 3,000 cycles, if it does not exceed the new, lower TLM cyclic limit. The CAA has classified this service bulletin as mandatory and issued AD 006–05–2001 in order to assure the airworthiness of these Rolls-Royce plc. turbofan engines in the U.K.