NACUSO

THE NATIONAL CENTER FOR
COLLABORATION & INNOVATION

February 1, 2012

Ms. Mary Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Re: Proposed Amendments to 12 CFR Parts 701 and 741 – Loan Participation Rule

Dear Ms. Rupp:

NACUSO has considered the effect of the proposed changes to the Loan Participation Rule upon CUSOs and credit unions that work with CUSOs. On behalf of NACUSO, we would like to take this opportunity to share our thoughts on this proposal. As the sole association representing exclusively the interests of CUSOs and their credit union owners, we respectfully are of the opinion that there are several significant changes that need to be made in the proposal to better enable credit unions and CUSOs to continue to benefit from CUSO-centric business models that have proven over the years to be extremely effective in producing high quality loans and sharing both the risk and the yield in the loans among credit unions.

For example, the proposal prescribes that a credit union may not buy loan participation interests from a single originator that in the aggregate exceeds 25% of the purchasing credit union's net worth. There is no provision in the proposed amendments for credit unions to be able to seek a waiver from this new and potentially far reaching restriction.

Credit unions have formed mortgage and business lending CUSOs that close loans in either the CUSO's name or in an owner credit union's name with the originator selling loan participation interests in the loans to the CUSO's other owner credit unions. This very successful model enables credit unions to aggregate resources to hire experienced lending expertise at a much lower cost than if each credit union implemented the service internally. The credit unions perform the due diligence on the underwriting and control the servicing. The lending model is specifically designed to meet their strategic and business goals.

We have found that the creation of lending CUSOs with this business model results in a level of due diligence that tends to be much higher than transactional due diligence on a random credit union seller. After all this hard work developing such a structure, this proposal will cripple these CUSOs and their established method of operations. In fact, many credit unions involved in lending CUSOs will be out of compliance on day one following the enactment of the proposal and with little benefit in preventing systemic risk. Actually, the results could work contrary to the stated purpose of the proposal as these credit unions that will find themselves in immediate non-compliance are some of the credit unions that were proactive and did everything correctly to make performing loans to serve their members and share yield, liquidity and risk. If enacted, this proposal would be a deterrent to this type of collaborative, innovative and risk sharing lending solutions.

Loan participation interests will always be a source of yield to the credit union industry. If credit unions cannot fully realize the benefits of a CUSO-based solution, credit unions will search for other loan participation partners and will be forced by the one-size-fits-all 25% maximum in this proposed regulation to cut short their relationship with trusted credit union partners and deal with other credit unions they do not know as well. The additional due diligence costs of seeking new loan participation partners will be yet one more burden on the industry.

The fact that a credit union buys loan participation interests from a small number of originators does not by itself pose a risk as long as the credit union has done proper due diligence on the quality of the loans and the originator's lending practices. A safe originator will be safe for all buyers and a poor originator will be risky for all buyers. Prior to implementing absolute restrictions on transactions, we recommend that NCUA issue guidance (not a regulation) that would require due diligence on the originators that includes an evaluation of the delinquency rates on the types of loans being offered for sale and if the delinquency rate exceeds industry averages, the buying credit union should not purchase more than a limit specified by NCUA for a particular credit union through the examination and supervision process.

If there is a limit on loan participation interest purchases, we recommend that additional latitude be given buying credit unions that have demonstrated that the buying credit unions are well capitalized as defined by Prompt Corrective Action, Part 216 of the Federal Credit Union Act. Well capitalized credit unions have the capital to absorb risk and therefore the level of capital should be part of the risk evaluation prior to cutting off successful loan participation relationships.

While we understand that NCUA has certain situations needing additional scrutiny on loan participation agreements and performance in mind when making this proposal and agree that the examination and supervision process should focus itself on those situations requiring much closer monitoring, we believe that requiring the entire industry to bear additional burdens because of the acts of a few credit unions will not strengthen the industry. Frankly, it makes no sense to us that a CUSO could sell whole loans to a credit union as eligible obligations without purchase concentration limitations but be limited on the number of loan participation interests the CUSO can sell to the same credit union. This regulatory approach unnecessarily raises questions among credit unions about the value of the credit union charter to their strategic goals as it hinders the ability of credit unions to build capital.

If enacted as proposed, these amendments raise other questions with regard to the ability of credit unions to work with CUSOs. If a credit union buys loan participation interests both from a CUSO and a credit union owner, does that not raise the question of whether the purchasing credit union has a 25% net worth limitation from the CUSO and another 25% net worth limitation from the credit union owner; or would the two be combined? The proposal seems to be silent on this basic and crucial question. It is for reasons such as these that any concentration provision, including this concentration provision, should be subject to waiver for good cause shown.

We take this opportunity to recommend that credit unions be given the ability to sell loan participations in loans purchased under the eligible obligation rule. We recommend that a credit union that buys an eligible obligation be considered an originator for purposes of the 10% originator retention requirement. Otherwise loan participation interests in the loans that a credit union buys as eligible obligations can never be sold as the originator is no longer involved in the loan. Clearly the selling credit union would have "skin in the game." The fact that the selling credit union did not originate the loan is not a reason to prohibit the sale of a loan. We note that an originator does not retain "skin in the game" when it sells an eligible obligation to a credit union, yet it is permissible for the credit union to buy the whole loan.

Our last recommendation involves the situation where a credit union obtains a waiver, such as a waiver from the personal guarantee requirement. Currently, a credit union that buys a loan participation interest in such a loan must also obtain a waiver. That renders the loan participation interest unsalable from a practical standpoint. No buyer wants to go through the waiver process. We recommend that if the originator obtains a waiver for a loan, a credit union that buys a loan participation interest in that loan not be required to also obtain a waiver.

While this is admittedly a complex issue for many credit unions and CUSOs, the proposed regulation very likely will have a greater negative impact on the important principle of collaboration and risk sharing than it will have a positive impact on the handful of situations in which additional oversight and monitoring is justified. Again, NACUSO recommends that NCUA and state regulators address these individual situations through the examination and supervision process.

If NCUA feels that its supervision and examination authority over participating credit unions is not sufficient to handle the risk involved and a new regulatory solution is supportable, NACUSO strongly encourages the agency to significantly amend this proposal to take into consideration our position above as it relates to the inadvisability of the 25% participation maximum from one originator, the need for improvement in the waiver authority, the need for flexibility to permit the sale of loan participation interests in eligible obligations and the elimination of the need for duplicate loan waivers from buyers.

We thank you for the opportunity to comment on this important proposal.

Very truly yours,

Jack M Antonini

Jack Antonini, President

Cc. The Honorable Debbie Matz, Chairman
The Honorable Michael Fryzel, Board Member
The Honorable Gigi Hyland, Board Member