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FEDERAL CREDIT UNION
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February 3, 2012

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

Dear Ms. Rupp:

We appreciate the opportunity to comment on NCUA's proposal on loan participations. While we recognize that the goal of the proposal is to reduce risk, we strongly believe that several key provisions of the proposal will be damaging to credit unions and members and may have a number of unintended consequences. Our major concerns are as follows:

Limits options for credit unions and members

At a time when the credit union industry is asking Congress to expand its ability to lend by increasing member business loan limits, the proposed limit that no more than 25% of a credit union's net worth could be in participation loans with any single originator would have the exact opposite effect. Originating credit unions that have many long term arrangements with credit union participants who may exceed this threshold would have to scramble to seek out new participants to manage their loan portfolios, potentially making credit more difficult for members to obtain.

Added costs and due diligence

When a credit union decides to purchase participation loans from another credit union, it is a time consuming and costly process involving document review, legal fees and thorough due diligence. Our credit union, like many, has a few well researched and long standing loan participation relationships with other credit unions. We continue to purchase loans from a few selected players because of their quality and the performance of those loans and relationships over time. If external limits are placed on those participation relationships, it creates significant burdens and costs to locate other sources, assuming they can be found, in addition to diverting funds away from long standing relationships that are working extremely well.

<u>The proposal does not focus on the true source of risk on participation loans</u>

We purchase loans only from other credit unions, where the originator has always retained 10% or more of the loans that were sold to us. We have no qualms with, and see a true value in, requiring any originator to keep a portion of their loan. We feel that the proposed cap of no more than 25% of a credit union's net worth with any one originator, however, stems from a misunderstanding of the true risk area for loan participations.

The true source of stability or risk on any loan, participated or otherwise, lies in the quality of the credit underwriting and documentation. While we evaluate the financial condition of originating credit unions that we purchase participation loans from, the business reality is that even if a credit union becomes financially distressed, not only does NCUA almost always insure continued operations for the credit union, pending a merger or dissolution, but member loans that were properly underwritten continue to pay. For example, we had a participation arrangement with Members United Corporate FCU for residential mortgages in excess of the proposed limits. They were conserved by NCUA and the loans continued to pay. Had we been conserved by NCUA, the loans would have continued to pay. The quality of the underlying loan assets truly determined the level of potential risk far more than the financial status of either the originating or participating credit union.

<u>The 25% of net worth proposal actually creates more risk for credit unions</u>

As a teachers' credit union, our members are heavy savers. Consumer and business loan participation programs with a few well researched, long standing originating credit unions, have been a key component of our asset-liability management policy for several years. Like other credit unions, we currently have participation balances outstanding with some originators that are within our well defined and well thought out policy limits, but over the proposed 25% of net worth level. Many of these are member business loans that carry balloons and maturities between 18 and 36 months, which significantly reduces our long term interest rate risk.

We assume that NCUA's proposal, if adopted, would grandfather existing loan balances already on the books, as opposed to forcing credit unions to divest balances. Despite this, however, we would have significant loan dollars that could not be reinvested with originating credit unions within the next 12 months. As noted earlier, finding additional originators to participate with would be time consuming and costly, and there is no guarantee that we could even locate another option, since some of our current participation portfolio is in extremely high quality, but very specialized, member business loans. The alternative would be either placing significant dollar into low yielding investments, which would negatively impact our earnings, or offloading them into the one loan product our membership seems to have an appetite for – long term mortgage refinances. This would create significant long term interest rate risk over 15 to 30 year mortgage time horizons, where that risk is currently minimal because of our short term maturity provisions.

Proposal on different underwriting standards unduly restrictive

We are also concerned about the potential interpretation and impact of the proposal that a credit union could no longer purchase participation loans if the underwriting standards for the loans differed from their own. Underwriting standards for indirect auto loans, for example, can differ from other loan types. It is not practical for our credit union to offer indirect loans due to a limited SEG base and the costs vs. benefits of establishing a program, but the proposal could be used to prohibit us from purchasing indirect auto loans from another credit union, since we do not have established underwriting guidelines for the product. Likewise, we have purchased taxi medallion loans in the past, but do not underwrite them directly to our existing membership. Most credit unions often purchase loans that have differ from their own underwriting guidelines, not because they are not qualified to review them, but because they cannot underwrite them efficiently on a direct basis, or do not have access to enough of certain loan types in their market.

Recently NCUA's Executive Director, David Marquis testified before Congress on HR 3461 about examination protocol. In his testimony, he noted that "currently, much of an examiner's findings are based on sound judgment and sound business or industry practice," commenting that HR 3461would cause NCUA to issue numerous new regulations to address concerns "that are currently scaled using professional judgment, based on the size, complexity, and level of risk within the individual credit union." This was sound counsel to Congress and we strongly encourage NCUA to apply the same principle to its current proposal on participation loans.

A "one size fits all" approach often causes more problems than it solves. Different credit unions have different risk profiles and management expertise and need to be evaluated accordingly. A credit union with 12% capital could and should have different concentration risk policies and ALM strategies than one with 6% capital. In our case, we have historic delinquency and charge off levels that are a fraction of those of our peer group, which can and should drive to different decisions about how to manage our loan portfolio than another credit union with serious loan quality issues.

We are also unique for our $76 million asset size in that we have over 50 years of combined commercial lending experience and expertise on staff, where our ability to become involved in member business lending participations can and should differ from a credit union without that skill set. Over the years, our examiners have always applied the prudent standards and professional judgment mentioned by Mr. Marquis to our loan portfolio and business model, and we have appreciated the opportunity to have our credit union evaluated in a proper risk and experience context, as opposed to against a single standard being applied all credit unions, even though their size, complexity and risk profile might be vastly different.

We strongly encourage NCUA not to adopt the 25% of net worth with one originator proposal, as well as to continue to allow credit unions to purchase participation loans that may have slightly different underwriting standards than their own portfolio. If you determine that you cannot accommodate that request, we ask either that the percentage be increased to 50% as opposed to 25%, to allow credit unions more flexibility in managing their portfolios and relationships, or that a process be established where credit unions could request a waiver of the 25% of equity limit with one originator.

We understand your desire to seek ways to limit risk and truly believe that all of us in the industry share this, and other, common goals. We feel that the proposal as drawn, however, will create several negative and unintended consequences. We are truly grateful for the opportunity to provide feedback on this proposal as we all work together for the benefit of our industry.

Please do not hesitate to contact us if you have any questions about the feedback that we shared in this comment letter, or if we can be of assistance in any way as you move through your review process.

Sincerely,

William J. Sweeney
CEO

Michael Giles
Senior Lender

cc: Fred Becker, President - NAFCU
William Mellin, President - CUANY