We entered the Member Business Loan (MBL) market in 2003 and formed Credit Union Business Services LLC (CUBS) a business lending CUSO that today has twenty local credit unions participating in MBL's. CUBS is actively managed by seven owner credit unions as members of its board of directors. The portfolio equals $95,500,000 in investor and owner occupied properties with a composition of office, professional, industrial warehouse, retail centers, and flag hotels. Loan balances range between $140,000 and $12,000,000. We currently have no loans 30 days or more past due. Losses since inception (2003) equal 1% of outstanding loans. All properties are local (within our state or immediately adjoining), we meet with borrowers and inspect properties used as collateral prior to lending and inspect properties annually. Loans generated may come through one of the credit unions or other third party sources.

By necessity several of our larger credit unions originate many of the loans generated because of their branch penetration of the local area and their ability to serve their local business community. The 25% proposed limit to one originator would in short order limit the other credit unions in their ability to participate in higher yielding loans. The larger credit unions have established individual loan limits; the highest limit of one of the largest is $2,000,000. Lacking the ability to participate larger loans and diversify its portfolio i.e. a $5,000,000 loan request, the larger credit union would be forced to either decline to originate the loan or take more risk than it desires with one borrower. An unintended consequence of the proposal could be causing larger concentrations to one borrower or group of borrowers as credit unions choose to fund entire balances as opposed to participating larger loans.

The loan servicing is centralized and managed by credit union owners in CUBS. Servicing revenue offsets administrative and operational cost. Like the loans that comprise the portfolio, the servicing component is locally managed and controlled by the participating credit unions. Private servicing entities remotely located and beyond the control of credit union owners, presents a far greater risk than our current structure. Further, having a category of commercial or residential mortgage loan portfolios scattered among two, three or four servicers multiplies management responsibilities regarding due diligence, accounting systems and coordination with multiple parties and systems.

The two examples of grievous losses regarding MBL's most often quoted are Eastern Financial CU and Norlarco CU. Both examples are for loans used for speculative construction (properties built for the prospect of future sale) and at least one, if not both, had an element of fraud and a complete lack of oversight and due diligence invested in their loans and their borrowers. These excessive losses were not due to investor or owner occupied properties, stabilized and generating positive cash flows. Many of the credit unions who experienced losses in these projects were located in faraway states and performed little if any due diligence.

We understand the agency's desire to limit risk and protect credit unions but we would urge the agency to look at our example of how participations can be used effectively to diversify risk as intended in the original rule. The 15% of net worth limit to any one borrower or group of borrowers should be sufficient to limit undue exposure to one institution. Furthermore, regulations clearly indicate that participant credit unions should not rely on the originator to assess credit quality, but rather, each participant conduct its own independent evaluation. If limits are going to be instituted, perhaps we should target the weaknesses that have presented losses like “speculative construction loans” or loans “generated out of the credit unions area of operation.”

In a period when the industry and the agency are struggling to increase the 12.25% of total asset limitation to permit credit unions to add loans to their MBL portfolio, does it really make sense to impose more restrictions further limiting credit unions and their ability to lend to small businesses in their area of operation?

Fraud and theft by borrowers and servicers and lack of due diligence by a few credit unions should not be used as the basis to impose restrictive regulation on the rest of the industry. Additional regulation will not prevent losses by theft or poor management practices.

I urge you not to implement the proposed 25% of net worth limit to one originator.

Gary Nalley
Managing Member
Credit Union Business Services LLC