Tech CU TECHNOLOGY CREDIT UNION

August 25, 2015

Barbara B. Kamm
President and CEO

Gerald S. Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street,
Alexandria, VA 22314-3428

Re: In support of
NCUA 12 CFR Part 723
RIN 3133-AE37
Member Business Loans; Commercial Lending

Dear NCUA Board Members,

We would like to commend the NCUA for the thought and deliberation that has gone into the Proposed MBL Rule, and we fully support its implementation.

Technology Credit Union has spent the past five years building a strong commercial lending practice in the San Francisco Bay Area with highly skilled commercial lenders and credit administrators making prudent credit decisions. We currently have no delinquencies in our commercial/MBL portfolio, and we have had no foreclosures or charge-offs on loans generated in the past five years.

The board and management of Tech CU made a strategic decision to develop a commercial lending practice for several reasons:

- We operate in the heart of Silicon Valley and the Bay Area, *the most entrepreneurial community* in the United States, and many of our members start and operate their own businesses. To retain their relationships, we must be able to serve their commercial needs as well as their personal needs.
- We wanted to diversify our credit risk away from the credit union's traditionally strong reliance on residential real estate and consumer loans because of the huge impact the Great Recession of 2008 had on those sectors. We feel a commercial portfolio equal to about 30-35% of total loans would be appropriate to provide that diversification.
- We wanted to improve our yields with such products as SBA loans, construction loans, and asset-based loans because the commoditization of residential real estate and consumer loans has driven pricing on those products to a very low level.
- We wanted to improve our Asset/Liability Management with the variable rates and shorter maturities characteristic of commercial loans, and
- We had the experience and reputation in the market to attract the talent needed to be successful.

We operate in a fiercely competitive marketplace here in the Bay Area that includes at least 85 other financial institutions, many of which concentrate on commercial lending. And we've found ourselves at a significant disadvantage in getting ***the best*** commercial loans with the ***strongest*** borrowers because of many of the constraints imposed on Member Business Lending, including:

- The limitation on unsecured loans

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- The limitation on nonrecourse (unguaranteed) loans
- The limitation on construction and development loans

We have spent many unproductive hours preparing waiver requests to submit to the California DBO and the NCUA to get a little bit of relief in those areas, and we have also spent unproductive and expensive hours with attorneys trying to do the right thing in interpreting some of the confusing NCUA regulations, only to find that we somehow still got it wrong and had to spend even more unproductive hours submitting forbearance requests. In some cases, this work was needed because of differing interpretations we received from NCUA staff. We recognize that all the work at our end requires staff at the CA DBO and the NCUA to spend similar amounts of time and effort reviewing our requests, which diverts attention from more critical regulatory issues. This craziness needs to stop, and we need to get back to the business of serving our members.

We applaud the NCUA for developing the proposed revision to the current MBL regulations, and we strongly support the elimination of the current MBL waiver process and a prescriptive rule in favor of a principles-based rule. We have reviewed the proposal and have some comments that we hope will contribute to making the rule more relevant and effective for those that are actively engaged in commercial lending. But before we discuss those suggestions, ***we strongly urge the NCUA to do whatever it can to eliminate or increase the MBL lending cap.*** This cap is harmful to credit unions and their members in many ways:

- It prevents the proper diversification of the total loan portfolio (as stated above, we believe a portfolio of 30-35% commercial loans is best).
- It forces credit unions to be less competitive from a pricing standpoint and take more credit risk because, if you only have a small bucket to work with, you want to try to fill that bucket with the best priced loans. Often, the higher priced loans reflect lower credit quality, because top quality borrowers can get the lowest pricing in the marketplace.
- It encourages credit unions to buy nonmember loan participations from other credit unions to absorb liquidity, use staff effectively and stay under the cap. If done carefully with competent and trusted partners, loan participations can be a good strategy, but they can present significant credit risk when the loans aren't properly underwritten, monitored, and collected by the selling credit union.
- It threatens the jobs and career paths of the commercial lenders who see a looming cap and are concerned they will soon be out of the lending business. This makes it very difficult for credit unions to keep top staff and maintain strong relationships with their borrowers.
- "Managing the cap" and related activities, like buying and selling loan participations, cost time, effort and money that could be used more effectively and productively for our members on other activities.

If the MBL cap itself cannot be increased or removed, **we urge the NCUA to focus on the statutory constraints of Section 107A of the FCU Act** which limits the aggregate amount of MBLs that a credit union can make to the lesser of 1.75 times the actual net worth of the credit union or *1.75 times the minimum net worth* required under the FCU Act for a credit union to be well-capitalized. This means we must use only 7% to calculate our cap when we have a net worth of 10.85% and we endeavor to keep that ratio above 10%. If we have to calculate a cap based on net worth, it should be based on our own net worth, not some mythical number.

And finally, on the statutory side, if we are forced to keep the cap, **we encourage the NCUA to push for the removal of the 1-4 family non-owner occupied residential loan from the MBL cap**. No other commercial lender has to count such loans as commercial loans.

Regarding the proposed rule:

1. Page 16 and Pages 22-23 provide definitions of "associated borrower" and "common enterprise."

   We recognize the effort to be consistent with rules applicable to banks, however, the bank rules are complicated and confusing, often requiring legal interpretation, and we would encourage the NCUA to try to simplify these definitions, or at a minimum provide examples to help us interpret the definitions.

2. The definition of "control" on page 23 states that control exists when "one or more persons or entities: (1) owns, controls, or has the power to vote 25 percent of more of any class of voting securities..."

   While we understanding that the rules applicable to banks also use the 25 percent control rule, we submit that actual control does not happen until the parties have over 50% of the voting power and question the use of 25 percent.

3. Page 18 – "the proposed definition clarifies that the denominator of the LTV ratio is the market value for collateral held longer than 12 months, and the lesser of the purchase price and the market value for collateral held 12 months or less."

   We have run into this issue here in the Bay Area because the values of commercial properties have moved dramatically in recent years. Given that we use fully-competent and professional appraisers AND we have independent, third-party reviews done of those appraisals, we believe that to remain competitive in this type of marketplace, we should be allowed to use the market (appraised) value of properties held less than 12 months. We temper the movement in market prices by usually requiring that such loans have a fairly conservative, 55-65% LTV.

4. Page 35 – "the proposal eliminates prescriptive risk management requirements for LTV ratios, minimum equity investments, portfolio concentration limits for types of loans, and personal guarantees. .... The removal of the prescriptive requirements from the rule does not relieve the credit union from setting appropriate limits as part of its overall commercial lending program."

   While good portfolio management may call for setting limits on certain types of loans, we would point out that there are no regulations in the banking world for setting limits on unsecured loans or unguaranteed loans. The only limitations we are aware of are the 100% of total risk based capital for construction, land and land development loans and the 300% limit on non-owner occupied CRE loans. We urge the NCUA to refrain from being prescriptive in requiring too many limits.

5. There are several places where the proposed rule calls for certain things to be in policy that are more appropriate in standards or guidelines. For example, on page 38 – "policy must address the required analysis and depth of the financial review performed to support the credit decision." And on page 39 – "The policy must establish due diligence requirements....It should address the minimum criteria for historic reporting at the inception of the loan...."

   We believe policies should be kept at a high level and would like to see these and similar prescriptive sections rewritten to allow credit unions to place this level of detail in our standards.

6. Further in a prescriptive vein, page 40 states, "For more complex and larger borrowing relationships..., the credit union should require borrowers and principals to provide either (a) an auditor's review of the financial statements... or (b) an independent financial statement audit...."

   How do you define "complex and larger?" We find that many good borrowers, particularly those involved in multiple, complex real estate transactions, do not have reviewed or audited statements, and we would be uncompetitive in the marketplace if we were to require them. We believe that the determination as to what type of financial statement is required should be spelled out in the credit union's standards and based on the credit analysis of the specific transactions, not prescribed in the rule.

7. On page 41, we noted the following comment: "Unsecured commercial lending presents additional risk to the lender. Such lending *should be limited and treated as an exception*, to be offered only when the additional risk is adequately offset by appropriate risk mitigants."

   Prescribing that unsecured lending should be limited and *treated as an exception* undermines the point of allowing unsecured lending. We recommend that management should be allowed to set appropriate limits for unsecured lending and that the term "exception" not be used to describe unsecured loans. Policy should allow for the use of unsecured lending in those instances where the additional risk is adequately offset by appropriate risk mitigants, and standards should more closely define what the credit union considers appropriate.

8. On page 54, we note the statement, "...while the minimum net worth requirement for most credit unions to be well-capitalized is the 7 percent leverage ratio, it can be a higher amount if a credit union is subject to a risk-based net worth requirement..."

   Point of information—is this saying that we will automatically get a higher lending cap if RBC II is implemented?

9. On page 55, two types of loans are described that are defined as commercial loans but not MBLs, including "Loans in which a federal or state agency...fully insures repayment, fully guarantees repayment, or provides an advance commitment to purchase the loan in full."

   One would expect that this is what allows the guaranteed portion of SBA or USDA or other government-guaranteed loans to be excluded from MBLs; however, we must note that an SBA loan is NOT fully guaranteed—only 50-85% of the loan is guaranteed. Please clarify that the guaranteed portion is excludable from MBL totals, even though a portion of the loan remains unguaranteed and is counted in MBL totals (unless the NCUA will allow us to exclude the entire amount of such loan).

   We would also note that this should specifically include the 2nd Trust Deed portion of an SBA 504 loan, since we do not fund such loans until the SBA issues us a commitment to create a debenture that would take us out of the 2nd TD loan. While the 2nd TD loan is usually on the books for a short period of time (60-90 days), in some cases where construction is involved, it could be longer. Being able to exclude that 2nd TD loan from MBLs before its takeout by a debenture would be helpful.

10. The footnote on page 55 states that "credit unions are currently subject to a regulatory requirement to seek prior approval from the NCUA for non-member loan balances to exceed the lesser of 1.75 the credit union's net worth or 12.25 percent of the credit union's total assets."

    We applied for and received a non-member loan cap of 7.75 percent several years ago. Can we assume this cap will fall away when we implement the new rule and that we will no longer be limited to 7.75 percent of our assets?

11. On page 58, it "identifies those credit unions that are, by statute, exempt from the aggregate MBL limit. Specifically, it provides that credit unions that have a low-income designation...are exempt from compliance...."

    As a credit union that was founded at a semiconductor company in Silicon Valley and chartered to serve the technology community, we will never qualify as a LICU under the current 50% + 1 rule because our demographic earns a very competitive wage. It has been suggested that we consider buying branches in the Central Valley to pick up poor members, but that goes against our strategic grain. It has also been suggested we buy exclusivity to sell to students on college campuses. We work extensively with schools, colleges and universities in our area, but we are competing with many other financial institutions, including all of the big banks, for the hearts and minds of students, and we are not willing or able to pay the exorbitant fees required to buy enough student members. Consequently, as one of the most skilled commercial lending credit unions in an area that boasts the highest level of entrepreneurship in the country, we remain saddled with an unrealistic MBL cap.

    We ask that the NCUA consider redefining a LICU for purposes of MBL loans as those credit unions that have 30%+ in low-income members. We do not need nor want the other benefits given to LICUs.

12. On page 57, the proposal provides that a federally insured credit union's net member business loan balance is determined by calculating the outstanding loan balance plus any unfunded commitments, reduced by....a lien on the member's primary residence...."

    This needs to be clarified. We make a number of loans where the primary residence is taken as an abundance of collateral or an abundance of caution. The lien usually reflects the full amount of the loan, although the equity in the property may be slim or non-existent. Would the full amount of the loan then be eliminated from MBLs, or would the MBL be reduced by the amount of equity in the property? And if this were an SBA loan, could we still reduce the unguaranteed portion by the amount of the lien or the equity in the property?

13. Regarding State Regulation of Business Lending, we have considered the options presented in the proposed rule, and we support Option C which grandfathers the states with MBL rules previously approved by the NCUA Board and permits states to submit new MBL rules for NCUA Board Approval.

14. We understand that the Board wants to delay implementation of the final rule for 18 months because it believes the "principles-based rule represents a significant change in approach." And the delay will allow credit unions to make necessary changes to their commercial lending policies, processes and procedures," while also allowing the NCUA and state supervisory authorities adequate time to adjust.

We would submit that the proposed rule does not represent a significant change in approach for Tech CU or for our very experienced lenders and credit administrators who have all come out of the banking arena. We have spent considerable time over the past five years developing our commercial lending practice to conform as closely as possible to what we are familiar with in the banking world, and much of what is described in the proposed rule is how we operate today. We have sought and received waivers relating to unsecured loans, nonrecourse (unguaranteed) loans, and the construction loan cap, and with some minor modifications to policies and standards, we would be prepared to make the change immediately. We are fortunate today to work with a very experienced MBL examiner in Region V, and we would expect that he, too, would be able to work with the new rule immediately. Consequently, we request that we be considered for immediate implementation following final approval.

15. On pages 94 and 95, the proposed rule states that a "federally insured credit union that elects to make a construction and development loan must also assure its commercial loan policy meets the following conditions:....(3) Release or disbursement of loan funds occurs only after on-site inspections...."

    This works for hard-cost draws, but generally not for soft costs. We would recommend that this distinction be noted. Also, we note that this is another condition that should not reside in policy, but rather is more appropriate in standards.

We again want to thank the NCUA for crafting this proposed rule and ask that consideration be given to our comments. Please do not hesitate to contact us if you have any questions or seek any clarification.

Sincerely,

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