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August 28, 2015

Mr. Gerald Poliquin
Secretary to the NCUA Board
1775 Duke Street
Alexandria, VA 22314

Re: Comment letter on the Proposed Amendments to NCUA's MBL Rule

Dear Mr. Poliquin,
I appreciate the appropriate, prudent, and timely proposed changes resulting from the Regulatory Modernization Initiative. The opportunity to provide comments is also appreciated. Accordingly, I hope to provide some constructive comments based on my 20 years of commercial lending experience in the banking industry, 10 years of experience in running a small MBL CUSO out of the Chicago market, and communication with other business CUSOs throughout the country.

The expressed intention is perhaps the most positive development to date affecting the Credit Union Industry's current and future delivery of financial services to businesses, and well defined:
"Oversight will focus on the effectiveness of the risk management process and aggregate risk profile of the credit union's loan portfolio, as opposed to compliance with prospective measures... The proposed rule would provide federally insured credit unions with greater flexibility and individual autonomy in safely and soundly making commercial and business loans to meet the needs of their membership."

This new focus is a source of optimism among MBL CUSOs and Credit Unions actively involved in serving the needs of business members. There is some trepidation, however, in how the new approach will be implemented by examiners responsible for interpreting the Final Rule and how that will impact their exams. If the primary intention is as expressed, the optimal outcome would be that the "Supervisory Guidance" in practice, follows the intention of "greater flexibility and autonomy" to entities serving member businesses, provided "effective risk management" is governing their approach to extending credit.

Along this same argument, the detail provided in the Proposed Rules on specific items that need to be included in Lenders' Loan Policies appears to imply a "prescriptive" approach. Ideally, Credit Unions and member business services CUSO's would have the autonomy to draft policy consistent with the products and services intended to be provided, as well as, the needs of its members, while addressing the issues delineated in the proposed changes, with adequate flexibility to reflect that institutions unique culture and market. To this point, in past examinations of our Loan Policy, we have had examiners review and recommend very specific language, when the intention of the proposed language was already an integral part of the Policy.

With regard to specific provisions of the Proposed Regulation, I would offer the following comments, some of which you may have already received from my colleagues:

Common Enterprise and Control – The Proposed Regulation is confusing, difficult to manage, and seems inadequate. The 50% Common Enterprise Rule and the 25% Control Rules require more analysis than is practical. The most conservative approach, and the most practical, would be to count any borrower who has a joint interest with another borrower or entity as an Associate Borrower.

Calculation of the MBL Cap – The Proposed Regulation eliminates the 12.25% of assets Cap, with the sole definition of the MBL Cap changed to "the lesser of 1.75 times a credit union's net worth or 1.75 times the minimum net worth requirement to be considered well-capitalized." The proposed change is appropriate and well-intended. In the interest of compliance, the language should include detailed specific calculation of the term "well capitalized", or reference to the regulation defining this term.

Classification of an MBL vs. Commercial Loan – This distinction appears unnecessary, confusing, and difficult to manage. In reading the Proposed Regulation, loans that are included and excluded in these two definitions seems too complex. To be consistent with Banking language, it would seem appropriate to replace the term "Member Business Loan" with "Commercial Loan". For simplicity and to assure compliance, loans are either commercial loans or they are not. For example, 1-4 family residential and vehicle loans for household use are not considered commercial loans in the banking industry and should be regarded the same in the credit union industry. Similarly, a purchased participation in a commercial loan is a commercial loan with all the risk and required monitoring of any other commercial loan.

Non-Member Participations – The Proposed Rule excludes loan participations purchased from the MBL Cap and allows each credit union to set its own portfolio limit on the amount of non-member participation loans that can be purchased. This proposal conflicts with the experience the Credit Union Industry suffered through during the Great Recession, when a few large syndicators of commercial real estate loans impacted a wide range of credit unions that purchased these loans as investments, with little knowledge or experience in the complexities of commercial real estate lending. Under this proposal, credit unions could potentially buy as many non-member participations as desired. More alarming is the potential communication to the financial services community that would allow predatory lenders to sell as much as they want. These participations are often complex and far outside a credit union's geographic field of membership or home state. From a safety and soundness perspective, it would seem to carry more risk for a credit union to hold a large amount of its portfolio in non-member participations, while they are constrained by the MBL Cap on member business loans within their core market area. In point of fact, a recent regulatory review paper validated this in its review of bank failures during the Great Recession, concluding that many banks with high levels of non-owner occupied commercial real estate loans either failed or threatened safety and soundness as commercial real estate market valuations significantly declined.

It would seem prudent that the Final Rule include similar direction to what was provided to the banking industry by their regulators in the *2006 Interagency Guidance on*

Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices. In that publication the OCC, FRB, and FDIC strongly suggested commercial real estate concentrations held by banks be limited to 300% of net worth and construction loan concentrations be limited to 100% of net worth. The Interagency Guidance did not mandate these levels though, but went on to indicate that failure to abide by these limits could subject the offending institution to increased regulatory scrutiny.

Loan to Value Ratio – The Proposed Rule indicates the "value" be determined as "fair market value for collateral held longer than 12 months, and the lesser of the purchase price and the market value for collateral held for 12 months or less. The Board intends this clarification to ensure that credit unions have appropriate collateral protection in the event that the appraisal is inflated or the borrower overpays..." The proposal belies the extensive efforts undertaken by regulators to assure appraisals are performed properly and accurately. In addition, for commercial real estate appraisals, the Uniform Standards for Professional Practice sets high standards to assure appraisals are accurate. Assigning a prescriptive definition implies the appraisals cannot be trusted, and further, imposes restrictive limits for all transactions involving collateral held under 12 months. Such an approach is neither necessary nor effective in reducing collateral risk. Appraisals should be regarded as a reliable and appropriately reflecting the market values at the time of completion, while cost can be arbitrary, depending upon the relationship between the buyer and seller. The distinction included in the language appears unnecessary.

I sincerely appreciate the opportunity to provide input on NCUA's proposed rulemaking amending the Member Business Loan regulations. Please feel free to contact me for clarification or further discussion on any of these items.

Sincerely,

Daniel S. Bleil
President
Spectrum Business Resource, LLC