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August 26, 2015

Mr. Gerard Poliquin  
Secretary of the NCUA Board  
1775 Duke Street  
Alexandria, VA 22314

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

Dear Mr. Poliquin:

CEFCU appreciates having the opportunity to comment on NCUA's Notice of Proposed Rulemaking for 12 CFR Part 723 in regards to changes in the Member Business Loan regulations. We praise the Board on considering changes to regulation that would allow credit unions to better serve the needs of existing and prospective business members.

CEFCU has offered business services, including loans, to local businesses since the mid 1990's and currently has a portfolio of outstanding business loans in excess of \$315 million. It has always been our philosophy to serve as a "one stop shop" for the financial services needs of our members and this includes the individuals that own businesses and investment properties. As a well-capitalized credit union with over \$5 billion in assets, our Board of Directors and Management have built a Business Services department that provides members a reliable and trustworthy program with the products and services they need to be successful. As we continue to improve and grow in this area, the safety and soundness of the organization has always been a key factor in all the decisions that have been and continue to be made. This is reflected in the capital ratio of over 11% that is net of the \$107 million being paid out to our member/owners in the form of extraordinary dividends in the past 10 years, while maintaining a competitive rate and fee structure for both savers and borrowers.

We have always been understanding of the prescriptive measures in regulations that are specific, easy to understand, and consistently applied to all credit unions. For example, the aggregate of the net member business loan balances for all construction and development loans must not exceed 15% of net worth. Although it is applied to all credit unions in the same manner, despite their capital adequacy, asset quality, management, earnings, and liquidity/asset-liability management, this was easy to measure and manage. In addition, we recognize that when one of these regulations is a burden to credit unions ability to serve members that NCUA will listen and make changes as needed. For example, under 722.3(a)(5) (Appraisals

required) the variance between other financial institutions regulations and credit union regulations was simply the difference of the use of “and” instead of “or”. NCUA recognized how this inhibited our ability to serve members in a similar manner to other financial institutions and at a cost that is equal to or less than competition and made the necessary change.

Our concern has been with the opinions and prescriptive measures of examiner staff that prevent the Board of Directors and Management from setting risk tolerances and overseeing the safety and soundness of the organization as it relates to policy, procedures, and processes. Most of these are with what we consider non-material Observations that become Findings with specific action requirements given by the examiners, which are reflective of managing the department. These findings/observations are given with reference to non-specific guidance in Letters to Credit Unions like “size and complexity of the portfolio” and “prudent”. With no specific measures, this leads to opinions and inconsistency in application.

CEFCU is in agreement with a shift to a principles-based approach that would allow the Board of Directors and Senior Management to establish adequate controls and provide sound governance. This could allow better service to the members than management decisions made either to meet a regulation or made by an examiner. If implemented in a proper manner, this would allow credit unions to better serve members by setting risk tolerances (as reflected in Policy and Procedures) and strategic goals based on capital adequacy, asset quality, management, earnings, and liquidity/asset-liability management.

However, without seeing the guidance that would be given to examiners, there is concern that individual examiners could actually get more involved in the management of these loans and lack consistency in application of this approach with other NCUA examiners. If that is the case, the unintended consequences of the prescriptive approach that caused credit unions to manage lending practices to regulatory restrictions will likely become worse as individual examiners provide their opinion and requirements for each institution as to sound risk management practices. In order to allow credit unions to have greater autonomy and flexibility to soundly administer, underwrite, and service commercial loans, the measurement of a credit unions risk management process as well as regulatory objectives need to be examined with specific measures that are not based on opinion. For example, the specific measures applied to each credit union should include the capital ratio for that organization and the specific and measurable risks to capital from the MBL portfolio. Broad measures such as “prudent risk management systems” instead of specific measures like “capital ratios” would lead to concerns with any guidance issued by NCUA to examiners and Credit Unions. Hopefully this guidance will include specific measures for “effectiveness of risk management process” and “aggregate risk profiles of a MBL portfolio”.

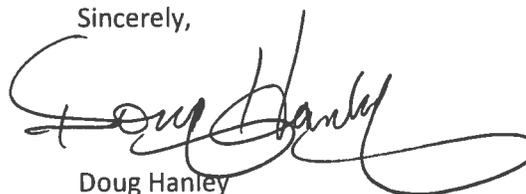
Here are a couple of examples where vague language could lead to varying opinions and the future guidance could eliminate that potential issue:

- 1) The proposed loan to value ratio incorporates what CEFCU already has in procedures for Real Estate by using the lower of cost or appraised value for property owned for 1 year or less. While CEFCU has further restrictive measures to ensure the borrower has “skin in the game”, those measures may not reflect the risk tolerances of other Credit Unions and are subject to change for CEFCU as our risk tolerances change. We support the proposed valuation method for up to 1 year from the purchase date for real estate collateral. For non-real estate, it is difficult to capture new relationships with a requirement to obtain a market value on non-real estate assets. Sometimes it may be virtually impossible to get someone to provide a market value. The risk of this varies with the size of loan, credit union profiles, etc. CEFCU has accepted the book value using straight line depreciation within generally accepted accounting principles (GAAP) to determine value. This uses the economic life of the asset and ensures that the loan balance stay at or below this book value, including no balances allowed on loans for assets that have been fully depreciated using the straight line method and does not punish the borrower that chooses to take advantage of an accelerated depreciation to save on tax liability. If a borrower wants the lender to consider a value greater than the straight line depreciation method, they would have to accept the cost and delays in obtaining a market value from a reliable source, as determined by the lender. Hopefully your guidance will be specific enough to indicate what qualifies as prudent and accepted commercial lending practices for determining market value of non-real estate collateral to put all credit unions on a level playing field and allows them to be competitive with other financial institutions.
- 2) CEFCU appreciates the clarification of qualified costs for construction and development lending. Most of this is very specific and easy to interpret. However, we would like to see guidance on specific methods for setting limits on any costs that are permitted if reasonable in comparison to the cost of similar services from a third party.

In conclusion, many of the provisions of the proposed rules could enable CEFCU and other credit unions to operate a more efficient MBL program while maintaining good governance to ensure safety and soundness. This will also help level the field for competing with the local, regional and national banks as well as other non-traditional financial institutions. However, the guidance that will accompany the proposed rule will determine the final impact and this should be subject to review and comment by credit unions prior to deciding on a final rule. Notwithstanding the concerns with the lack of guidance to accompany the proposed rule changes, CEFCU supports this proposed rule and congratulates NCUA for taking this approach.

Thanks for the opportunity to express our views and if you have any questions or comments, please do not hesitate to contact me.

Sincerely,

A handwritten signature in black ink, appearing to read "Doug Hanley". The signature is fluid and cursive, with a large initial "D" and a long, sweeping underline.

Doug Hanley

Vice President Business Services