BANKING – THE DCU WAY

July 24, 2015

Mr. Gerard Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314-3428

Re: 15-EA-16 NCUA – Member Business Loans & Commercial Lending Proposal.

Dear Mr. Poliquin,

As the Senior Vice President of Member Business Lending of Digital Federal Credit Union I am pleased to have the opportunity to provide comments on the proposed MBL rule changes. We previously have gone to our regional director to ask for blanket waivers and we appreciate his approval of these waivers as requested in a timely manner.

I am totally in support of making the changes to the MBL regulations that give the credit unions flexibility and individual autonomy to safely and soundly provide commercial and business loans to our members.

In my opinion the regulations originally were implemented because of the lack of sophistication and knowledge of MBL lending in the credit union industry before 1998. I was in the banking industry in Rhode Island in the 80's and observed the credit union problems that occurred from MBL lending abuses. So I understand the reasoning at the time for the regulations being written on the conservative side. But we are in the year 2015 and as over the years I have met and talked to at least 50 of my counterparts in other credit unions I find many experienced and well-seasoned commercial bankers running MBL programs. I have also notice that many credit unions have taken advantage of the numerous MBL educational opportunities that have be made available through NCUA, CUNA, NFCUA and other organizations. I have in fact been a frequent speaker at MBL educational events though out the country.

I do have some specific comments regard the proposal:

<u>723.2 - Definitions</u>

<u>Direct benefit</u> "…proceeds are used to acquire property, goods, or services."

> I believe that "property" should be replaced with "tangible and intangible assets". The word "property" sounds like real estate. Tangible and intangibles assets would include not only real estate but furniture, fixtures, equipment, portions of ownership (buying out a partner), buying rights to a product or service, contracts, etc.

<u>Common Enterprise</u>

> "The expected source of repayment for each loan...is the same for each borrower and no individual borrower has another source of income from which the loan…may be fully repaid." I am very unclear as to what this means. If we have two completely unrelated trusts, each having their own loan with us, if their only source of income for each trust is dividends from Microsoft, then would they be a common enterprise under this rule? An example would be very helpful.

<u>Control</u>

> "…has the power to vote 25 percent or more…" Someone with only 25% control really can have no control. I have two suggestions for change: Option 1 is to change it to "over 50%". Or option 2 is to delete it entirely and use points 2 and 3 in this section to cover the situations where an individual owning less than 50% really controls the company. Also I

think you need to eliminate situations where there has been a receiver assigned or an attorney has Power of Attorney due to death or other situations where the "person in control" is only temporary and/or a non-beneficiary.

Loan-to-value

"...lesser of purchase price or market value for collateral held 12 months or less…" I believe that purchase price should be used for the loan-to-value only when the funds of a loan are used to purchase the collateral. The 12 month requirement should be eliminated. If the collateral is already owned, even if only owned for less than 12 months, market value should be used in the denominator. Here is an example when the proposed rule would not fit: I buy a piece of land for $100,000 with cash, do some site preparation, get permits to subdivide, and obtain leases all in the first 6 months. The value of the land is most likely significantly higher than $100,000. The market value in this case would be the appropriate value for lending purposes. A second example would be related to inventory lending. Take a plastics' molding company buys resin at $1 per pound and for $2 of labor and overhead molds it into a medical device. Normal C&I lending criteria would say the collateral value is $3, but under the new rule one could interpret that since the resin is less than 12 months old and additional costs improving the collateral do not count, the collateral value is only $1. If the proposed rule is held at 12 months at least the value should be changed to "purchase price plus any cost of improvements".

723.3 Board of directors and management responsibilities

(2) Qualified lending personnel

"…must employ qualified staff…" I think the word "staff" should be changed to "management and loan officers". As written, the staff must have experience (albeit [3} allows for training) in all three areas (i) - Underwriting and processing, (ii) – Overseeing and evaluating the performance of a commercial loan portfolio, and (iii) - Conducting collection and loss mitigation. While the management should have experience in all three areas, the staff will not necessarily have all three. For example a credit analyst will not have, nor needs training for, collections.

(ii) "Overseeing and evaluating the performance of a commercial loan portfolio…"

This section sounds like a management's responsibility to the whole portfolio. A suggested change would be "Overseeing and evaluating the performance of individual commercial loan portfolios by loan officers and overseeing and evaluating the performance of an entire commercial loan portfolio by management…"

723.4 Commercial Loan Policy

(3)Projections. "…a projected balance sheet and income and expense statement…"

This is fine for C&I loans but in normal Real Estate purchase financing projected balance sheets are not required as they add no value. Certainly a projected income and expense statement is mandatory for a real estate deal. The wording could be changed to ''Projected income and expenses and other projections normal with the transaction of this type must be obtained."

723.5 Collateral and security

(a) "A federally insured credit union must require collateral..."

As you state later in the paragraph unsecured loans can be made. My suggestion would be to start the paragraph stating that the credit union can make unsecured loans with proper reasoning documentation. Then follow up with "if a borrower does not qualify for an unsecured loan then the credit union must require…"

723.6 Construction and development loans

I am very happy with this section as it mirrors the available construction and development loans in the industry.

723.8 Aggregate member business loan limit

(e) "…**form 5300 reporting…net member business loan balance is determined by…reduced by any portion of the loan that is secured by shares in the credit union, or by shares or deposit in other financial institution, or by a lien on the**

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member's primary residence…" In the old regs loans "fully" secured by shares or deposits were not including in NMBLs. Now I assume that we would include the un-cash-secured portion of a loan. However in the new section 723.2 the "Commercial Loan" definition states, ineligible commercial loans are loans that were only fully secured by shares or deposits. It does not include the partial cash secured loans. I would think we should be consistent on both definitions.

(e) Goes on to say "…503 reporting…reduced by…a lien on the member's primary residence…" Should this not read "reduced by loans that are fully secured by a lien on the member's primary residence"? As it read it appears that any loan whether fully or partially secured by the member's primary residence is deducted.

In conclusion, based on the MBL experience now in the credit union industry I truly believe that when these new rules become effective the credit unions will use their new powers wisely to make safe and sound loans to their members. Please feel free to contact me should you have any questions.

Thank you for the opportunity to comment.

Best Regards,

Stephen K. Mackowitz
Senior Vice President
Digital Federal Credit Union.