

NORTH COAST CREDIT UNION

Community minded. Member focused.

RECEIVED
JUN 21 2016
DIV. OF CREDIT UNIONS

June 15th, 2016

Department of Financial Institutions
Linda Jekel – Director of Credit Unions
150 Israel Road
Tumwater, WA 98501

Re: NCCU Review and Recommendation for MBL Rule Changes

Credit Union Profile

North Coast Credit Union was originally known as Bellingham Public Employees Credit Union and was established in 1939 to meet the financial needs of Bellingham public employees. In 1998 we adopted a Community Charter and began operating as North Coast Credit Union providing financial services to the broader community in our primary market area of Whatcom and Skagit Counties.

During the past 77 years the credit union has grown to \$220,542,919 in total assets and \$152,335,725 in loans outstanding as of March 31st, 2016. Our loan portfolio includes \$47,023,607 in consumer loans, \$66,477,578 in 1-4 family residential loans and \$42,600,00 in commercial member business loans and unfunded commitments outstanding.

North Coast Credit Union mission statement is to use our collective resources as a community – owned financial cooperative, to support those we serve to become self-sufficient, prosper and to make the communities we live in stronger.

North Coast Credit Unions History in Commercial Lending

- North Coast Credit Union began formally originating commercial loans around 2007, under an initial commercial loan approval authority of approximately \$15+/- million which was based on 12.25% of total assets.
- Based on our most recent current commercial loan lending authority, based on 242.5 % of equity, our commercial loans and commitments outstanding have grown to \$42.6 million as of March 31st, 2016. The maximum aggregate loans to one borrower and related interests, is currently at \$3 million, based on the 15% of capital limitation. All aggregate loans in excess of \$500,000 require a formal credit presentation and majority approval by the Credit Union Senior

Management Loan Committee, which consists of the President and Chief Executive Officer, Executive Vice President, Senior Vice President-Lending, Vice President —Chief Financial Officer and Consumer and Residential Loan Manager .

- Since the inception of our MBL Lending Program, we have experienced no historical loan losses and as of March 31st, 2016 have zero delinquencies, as well as, no adversely classified commercial loans.

Commercial Lending Department and Years of Experience in Commercial Lending

- My personal lending experience which includes residential, commercial and commerce and industry lending covers 41 years, which includes senior and executive level management positions at community banks, regional banks, mortgage subsidiaries, national banks and for the past 3+ years with North Coast Credit Union.
- During my career, I've been engaged in the successful turn-around of numerous troubled banks with criticized loan portfolios into safe, sound and profitable financial institutions. Specific responsibilities included, but were not limited to Loan Committee Chairman, with individual loan approval authority up to \$5 million, commercial loans ranging up to \$20 million and have been directly involved in complicated commercial loan work-outs and related litigation during three protracted economic recessions.
- North Coast Credit Union MBL Lending team includes a seasoned commercial lender, two part time financial analysts, loan servicing manager and loan processor/document coordinator with collective commercial lending experience of 100 years, and average experience of 25+ years. Their lending experience includes community, regional and national bank environments. Lastly, they have solid technical skills, are familiar with the local market and community, as well as the members we do business with.

Loan Underwriting Standards and the Type of Business Loans we Underwrite

- North Coast Credit Union is a designated Community Development Financial Institution with a special commitment to provide financial services to community members who are considered unserved and/or underserved by traditional financial institutions.
- North Coast underwriting standards and philosophy are based on listening to community members needs and cooperatively working with them, to determine if a loan can be creatively and safely structured with a reasonable likelihood of repayment. The borrowers financial capacity, repayment willingness and collateral, combined with lenders critical thinking, analysis, knowledge and judgement are essential in structuring, recommending and approving loans which are likely to be repaid. As a secondary underwriting safeguard, most of our MBL loans have marketable collateral which can be voluntarily or involuntarily liquidated for repayment or of the debt.

- North Coast credit and underwriting practices include periodic financial and business monitoring of larger and/or more complex credits for appropriate identification of credit, financial and collateral risk. Our vigorous loan monitoring and annual loan grade review process enables us to establish appropriate loan loss reserves and encourages lender-borrower discussions, which is often beneficial to borrower and lender in minimizing loan defaults and potential loan losses.
- With full respect and appreciation to larger regional and national financial institutions, who dominate and support the larger commercial lending market, a major distinction between North Coast Credit Union and larger out of area regional and national financial institutions, is personalized critical thinking and judgement on each loan request, regardless of loan amount, type of loan, collateral and borrower standing. In contrast, most large financial institutions have a stricter set of prerequisite rules, out of area loan processing and underwriting guidelines, which sometimes results in loan denials to many good community members, who might otherwise be deemed creditworthy and bankable upon closer review and consideration.
- As a result of the " Great Recession " many smaller local community banks, who provided similar services and financing alternatives have been closed, merged into larger regional or national banks. The net result is a void, or reduction in the availability of credit and financing options for smaller commercial borrowers. The surviving local community banks, who are permitted to loan out almost 100% of their assets out to commercial borrowers, will continue to have a strategic and regulatory competitive advantage over credit unions. Under the proposed new rules, credit unions will be limited to a commercial lending asset concentration based on 175% to 300% of equity, which generally limits most credit unions to a maximum 30%+/- of their loan assets concentrated in commercial loans, assuming a 10%+/- capital ratio.
- North Coast Credit Union commercial loan products loans include, but are not limited to purchase, refinance development and construction for general purpose commercial and residential real estate, commerce and industry loans, other specialized outreach programs to the Latino community, as well as other underserved groups located within our local community. Special use and other more complicated credits are also considered on a case-by-case basis, provided, the financing request and loan structure is sound and we have the appropriate expertise to assist the member borrower.

Since inception of our MBL Program we have made the following commercial loans which reportedly were declined by other traditional lenders.

- Purchase money commerce and industry loans for the purchase of numerous semi-truck/trailers and controlled accounts receivable line of credit to a relatively new, but growing ethnic minority owned trucking and transport contracting business. The principals have also referred numerous

individual driver-owners to North Coast Credit Union for new and replacement semi-truck loans, who are paying as agreed, or who have fully repaid their loans, under voluntary and accelerated repayment terms.

- Cash out refinance of a fully leased duplex, where the loan funds were used to pay for business relocation and tenant improvements for a long term and established business. The loan was declined by other traditional lenders, due to historical friendly debt incurred when the business was managed by others outside the family. The business had been profitable for the past two years, with no outside debt and prior historical losses were self-funded by capital contributions. The business and guarantors met all debt service coverage ratios, equity expectations, favorable credit history and improving business model, since the principal and son had taken over direct management of the business.
- Short term seasonal line of credit targeted to the latino community who are involved in a summer farm produce program. A local non-profit provides favorable land lease, training and support, whereby they grow and market crops to supplement their income, as well as develop valuable technical and business skills.
- Numerous solid real estate loans to bankable borrowers with financial capacity and collateral that were subsequently denied by other by traditional banks during the great recession, simply because the proposed collateral was real estate, or the type of business, or business sector they were engaged in was out of favor.

In summary, all of these borrowers reportedly approached traditional financial institutions, but were summarily declined with little or no consideration to their individual stories or merits. In other words, in many situations the credit unions commercial lending activities only compliment and do not directly compete with traditional financial institutions.

Potential MBL Loans compromised by Regulatory Restrictions and Uneven Playing Field

Current credit union commercial loan regulations are significantly more restrictive than traditional state and national banks, which ultimately diminishes the local economic environment and limits the availability of financing to many good and bankable community members.

Most reasonable and knowledgeable people know that the availability of financing is essential to job creation, economic opportunity and prosperity for all members within our community. North Coast has had to pass on many bankable loans, due to credit union regulatory restrictions due to the following:

- Lower maximum loan limits to one borrower and related interests.
- Lower loan to value limitations on commercial equipment loans.
- Lower commercial loan authority and concentration limits -as a percentage of assets or equity.
- Lower loan limits on development and construction loans

- Inclusion of consumer oriented 1-4 family residential rental properties deducted from our commercial lending approval authority and limitations, which is contrary to traditional banks.
- Inclusion of non-member commercial participation loans deducted from our commercial lending approval authority and limitations.
- Extensive and time consuming regulatory lending exception rules and procedures in order to receive commercial loan waivers and increased commercial lending authority. This process provides uncertainty, time delays and discourages both borrower and lender.

Recommended Changes to Washington State Credit Union Commercial Lending Rules and Parity with New NCUA Commercial Lending Rules

- Increase loan limits to one borrower and related interest from 15% to 25% of capital.
- Increase loan to value limits for commercial equipment and related non-real estate loans to 100% of cost or value, whichever is less.
- MBL lending approval authority increased to 300% of capital provided the Credit Union is well capitalized and has demonstrated they have experienced staff, policies and procedures with satisfactory commercial loan safety and soundness exams.
- Increase speculative acquisition, development and construction loans from 15% to 30% of capital. Development and construction for owner CRE and apartments to be retained, leased or rented as long term asset should be excluded - as source of repayment is not a speculative sale.
- Exclude 1-4 Family rental properties from commercial lending underwriting and commercial loan limits. To be included in consumer 1-4 Family residential loans similar to traditional banks.
- Exclude non-member commercial participation loans from commercial loan limits.
- Eliminate loan waivers and exceptions. Loans in excess of real estate and non-real estate regulatory limits to be limited, reported, monitored with a deduction against the Credit Union capital.
- To the greatest extent possible the New Washington State MBL Rule changes should avoid detailed specificity, as to not be counter-productive to NCUA intent to move away from prescriptive lending practices.
- Provide Credit Union lenders with an opportunity to review and comment on WA State DFI recommended MBL changes in their entirety before issuing final proposed rule changes

Summary

North Coast Credit Union appreciates the Washington State Department of Financial Institution and National Credit Union Association efforts and progress towards improving the commercial lending regulations for Federal and State chartered credit unions.

We believe current economic, marketplace and changing social attitudes, as well as, borrower financial needs warrant these proposed changes, especially when you consider the number of

local community bank closures during the great recession and its impact on the availability of credit in smaller communities. While some traditional banks may oppose these changes, the remaining regulatory discrepancies between credit unions and banks, combined with their economies of scale and resources still heavily favor traditional banks and protect their strategic market advantage.

At the end of the day, even if a credit union receives commercial loan approval authority up to the maximum of 300% of equity, assuming 10%+/- capital ratios, this equates to a commercial loan risk concentration of only 30%+/- of total assets, which is very limited and is significantly less than traditional banks, who can choose to have the majority of their loan assets concentrated in commercial loans.

Having worked at community, regional and national banks, many of the loans originated by credit unions serve a different segment of the market, which are often excluded by larger traditional lenders. Many highly qualified commercial bankers have now joined credit unions, after becoming negatively impacted by mergers, disillusioned by out of area, or state centralized loan processing, underwriting and decision making, by people who are unfamiliar with the borrower, community or local market conditions. In addition, safety and soundness exams for credit unions commercial lending activities typically include existing or prior commercial bank loan examiners, with years of experience, which provides appropriate regulatory oversight to credit union lending activities.

In our opinion, the proposed changes do not make our financial delivery system weaker, but are complimentary and provide more and not less financing options for many bankable community members, who are willing to commit capital and resources, which provides jobs and makes our local communities stronger.

Cliff A. Frydenberg
North Coast Credit Union
Senior Vice President-Lending

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