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June 20, 2005

Mary Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

RE: Comments on Proposed Rule 723, Member Business Loans

Dear Ms. Rupp:

Members 1st FCU is seeking to comment on the NCUA proposed Regulation regarding member business loans that will change the definition of construction or development loans. Members 1st acknowledges that if not properly monitored or underwritten, construction or development loans pose a significant risk of loss to credit unions. The primary risks of loss with these loans are non-completion of the project and the failure of the project to succeed after completion. That being said, proposed Regulation is broad and overreaching and can have what we believe are unintended consequences should it be enacted and interpreted literally.

Members 1st FCU is in excess of \$1 billion in assets and our current regulatory limit for construction and development loans is slightly over \$13 million. Our total portfolio of business purpose, commercial and investment loans stands currently at over \$59 million. With the new definition of construction and development loans we would rapidly exceed our construction and development loan limit; we would be forced to turn away loans of good credit quality that are fully secured at 80% loan-to-value at closing with a solid repayment source. Below are examples of actual members and loans we would be restricted in serving if the Regulation is enacted:

An established Credit Union member is a real estate investor and has annual cash flow in excess of \$800,000 per year and a net worth of over \$8 million in order to service a debt load slightly over \$250,000 per year. The member financed an \$850,000 63-acre agriculture property that was a vacant residence and now leases the property with a possibility for future development. Under the new regulations, this 80% loan-to-value credit with a solid repayment source would count against the Credit Union's construction and development loan cap.

- A local fraternal organization located in the same town as the Credit Union headquarters for over 75 years is relocating to a new headquarters. In 2004 the organization purchased an 8-acre lot for \$730,000 at 80% loan-to-value. In the next two to three years the organization plans on coming to the Credit Union for a construction loan to complete the project. Under the new regulations, this 80% loan-to-value credit with a solid repayment source would count against the Credit Union's construction and development loan cap.
- A member of the Credit Union expanded his business in 2004 and purchased the assets and real estate of one of his suppliers. The business assets were purchased by his S-Corporation and the real estate was purchased by the member and his wife. This situation is a very common practice as businesses will arrange for the real estate and the business operations to be held by two different entities for liability and tax purposes.

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The regulations are unclear as to how real estate holding companies are treated. An example would be in a literal translation, where a real estate holding company is purchasing a land/building to lease it to a company owned by the same principals at a new or improved location. This type of financing could be interpreted as a construction or development loan. In the proposed Regulation the Credit Union would be limited in funding these transactions; yet, in the above example the Credit Union would not be limited in these type of transactions should the member come to the Credit Union a year later, after the property is already purchased and improved.

- A not-for-profit cooperative in existence for over 40 years that operates a swimming pool complex is updating their property. The collateral value of the property "as-is" is less than 80% loan-to-value; in excess of \$200,000 was provided to the organization at settlement for improvements. This organization was improving a property already owned for an income-producing purpose. The loan has a solid repayment source and was fully collateralized at loan closing. Under the proposed Regulation, this loan could be interpreted as a construction or development loan and the Credit Union would be limited in how many loans of this nature we could fund.
- A husband and wife are starting to purchase vacant 1-4 family residential properties in our market area. The family has income of over \$200,000 annually with minimal debt and the debt payments can be serviced with no income from the property purchased. Under the proposed Regulation, since they would be converting this property to an income producing property these loans would be classified as a construction or development loan.

Also, the proposed Regulation is unclear as to the level of improvements necessary relative to the loan request in order to be classified as a construction or development loan. For example, a local motorcycle dealership with property worth \$750,000 recently was approved for a \$400,000 loan at the Credit Union. Half of the project funds were to refinance existing debt while the other \$200,000 was for improvements and additions to the property. Under the proposed definition it is unclear if this is a construction or development loan and whether the whole amount - or just \$200,000 - is a construction or development loan. Also, it is not uncommon for a member to refinance a commercial or investment property while also taking cash out of the equity in a property, for the purpose of improvements to that building or another building owned by the same member. For example, the member owns Property A with no liens worth \$200,000. If the member takes a loan on Property A for \$100,000 to improve Property B the loan would be classified as a construction or development loan even though the loan would be fully secured at closing with a documented repayment source.

Under the current Regulations, Credit Unions historically have had losses at less than ten basis points. By attempting to solve a problem that does not exist, the proposed Regulation would severely restrict credit unions from serving their members. Members 1st recommends that loans with the following characteristics be excluded from the definition of construction and development loans:

- Loans that are fully secured with a documented repayment source at the time of settlement where no more funds will be advanced
 - Land acquisition loans for possible future development where repayment is not dependent on the success, failure or completion of the project
 - Loans to real estate holding companies who convert or improve the property to income-producing purposes by leasing it to an entity owned by the same principal(s)
 - Commercial or residential loans purchased as vacant real estate that will be leased in the future where repayment is not dependent solely on future rental income
- Loans funded for the purpose of real estate improvement to the same property or another property owned by the same member where the collateral value will not be diminished during the construction process

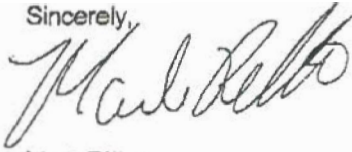
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Members 1st FCU has been extremely successful in serving our membership and the local small business community. These regulations would significantly deter our efforts of building a business loan portfolio in a safe and sound manner. We recommend the proposed Regulation be withdrawn to fully investigate the implications on the growing credit union member business loan industry.

Sincerely,



Mark Ritter
AVP-Small Business Lending