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Snyder, Diane L

From: Tom Wilson [twilson@centrisfcu.org]
Sent: Monday, June 20, 2005 1:14 PM
To: Regulatory Comments
Subject: Tom Wilson and Jackie Schwalen Comments on Part 723 MemberBusiness Loans

Dear Ms. Rupp,

I am submitting for your consideration the following comments on the proposed changes to 12 CFR part 723:

I do not represent a corporate credit union, therefore I will abstain from commenting on those changes that impact only corporate credit unions.

Definition of "Construction or Development Loans" - While one could reasonably debate the appropriateness of grouping these two distinct types of loans into one category, I will refrain from that discourse.

It is my understanding that the cap placed on these two types of loans was to limit credit unions from the additional risk these loans subject an institution to. For a construction loan, the time during which the facility is being erected provides more risk due to the potential of cost overruns, completion delays, etc. If the project is a passive investment, you also are subject to additional risk during the stage immediately following construction when the project is being rented/leased out. If the project is an active investment where the owner will occupy a portion (majority) of the facility, the risk is limited to the construction phase only (usually). Development lending has a greater degree of risk (potentially) than construction lending, since it is asset based. The risk is not limited to just the period of time when the property is being converted from undeveloped to developed but unimproved. The risk also is greater when you are selling these unimproved lots. While there are several techniques that can be employed to reduce the risk, the fact is, that this type of lending is generally riskier.

Whether the purpose of the loan was to acquire the property or whether it is currently owned, I believe that it should be treated as a Construction/Development loan as the risk is basically the same.

The definition of "Construction or Development Loan" as proposed is much too vague to accomplish the purpose for which it is intended without being overly burdensome for both the credit union community and its members. Based on the definition as proposed, if a member purchases a \$1,000,000 property to move their business into but wants to put \$50,000 of new carpet into it, that would qualify as a Construction or Development loan, as an improvement has been made to the property. The revised regulation does not address whether or not the improvement was material or whether it impacted the current use of the property. Rarely is the case that a business buys a building to move into that they do not have some improvements planned. Each business is so unique, that rarely is it the case that any existing building is "perfect" "as is" for its new owner. Not only will the regulation as proposed decrease member business real estate loans, it will also encourage practices that are not in the best interest of the members such as establishing escrow accounts for improvements instead of including the improvements on the loan and having the member use their funds for the down payment. In this case, the member will pay more in interest cost just so we can comply with the regulation and yet, the risk is the same in both instances.

Likewise, consideration should be given to how long a construction loan should be classified as a construction loan. The existing definition does not address that. Under the proposed (and current) definitions, a construction loan is treated as such for the life of the loan when in fact the additional risk exists only during the construction period. Based on my interpretation of the reg, a business can build a new facility and 12 months later when it is completed move into it. At that point, they can go down the street to another credit union and refinance the loan and it will no longer be treated as a construction loan but for the initial credit union it will be a construction loan the entire time.

In summary, I agree with the proposal to change the definition to include whether the property is acquired or currently owned by the member.

I would recommend that the definition for construction be changed to loans where the proceeds are used to convert a

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property from it's current use to an alternative use. I would also include that over 50% of the project cost must be used to alter the use of the project.

I would also recommend that you allow the loan to be reclassified as not construction once the construction phase is completed and the property has commenced it's alternative use. Land development loans will always be land development loans and should be classified as such. Loans where repayment is dependent on the liquidation of the collateral with no secondary source of repayment are by their nature of higher risk for their duration. They do provide a catalyst for other lending opportunities as well as community development, so given the experience of the credit union originating, should not be avoided altogether.

Lastly on this subject, I was unclear as to whether SBA loans ( and potetially, other government guaranteed loans) that are also construction loans would fall into this category. Since the use of the SBA/government guarantee helps to mitigate much of the risk associated with this type of loan I recommend that they be exempt from being classified as construction or development loans for the purpose of this calculation.

**Definition of "Net Worth"**- I do not envision that the proposed change will have a material impact to either our members or the credit union community. It would appear to apply some consistency in how certain calculations are made, so I do not oppose adoption of the proposed language.

**Government Guarantees-** I support adopting language that would allow us to use other government guarantees and that the collateralization and maturity limits that are allowed by those agencies also be accepted by NCUA.

Thank you for your consideration of our thoughts on these matters.

Sincerely,

Tom Wilson Vice President Commercial Products  
Centris Federal Credit Union

Jackie Schwalen, President  
CU Member Business, Inc.