

February 8, 2006

John A. Davis, Jr., Chairman
Kevin S. Dion, President
The Cypress Group LLC
921 North Mills Avenue
Orlando, FL 32803

Re: Cash Flow as Collateral for Member Business Loans (MBLs).

Dear Messrs. Davis and Dion:

You have asked if a borrower may assign cash flow as collateral to satisfy the loan-to-value (LTV) requirements of the MBL rule. Cash flow may be assigned as collateral for an MBL if its market value can be established and if its value is sufficient to satisfy the MBL rule's LTV requirements. Alternatively, a credit union may request a waiver of the LTV requirements if the cash flow cannot be valued or its value is insufficient.

Your company is a credit union service organization that provides business loan underwriting, documentation, and portfolio maintenance services. You state your credit union owners have received requests to make MBLs where the collateral will be an assignment of a cash flow stream, such as accounts receivable from a business. You have also indicated that you will take certain measures in connection with these loans to enhance safety and soundness. For example, you will analyze the historical and pro-forma financial performance of the borrower to determine creditworthiness and the value of the collateral.

With few exceptions, the MBL rule requires all MBLs be secured by collateral. 12 C.F.R. §723.7(a). This ensures credit unions have a secondary source of repayment if a borrower defaults on an MBL. The MBL rule's general LTV requirement is a maximum of 80%, although higher limits are permitted under limited circumstances. 12 C.F.R. §723.7(a)(1). The term "value" in the rule's definition of "loan-to-value ratio" is defined as the market value of collateral used to secure a loan. 12 C.F.R. §723.21.

While the MBL rule does not specify the kinds of collateral a borrower may use to satisfy the LTV requirement, collateral must have an ascertainable market value in order to meet the LTV requirements. If the market value of proposed collateral cannot be ascertained, then the MBL for which the collateral is offered as security cannot satisfy the LTV requirements.

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The MBL rule permits a credit union to seek a waiver of the LTV requirements for a category of loans. 12 C.F.R. §723.10(d). Seeking a waiver of the LTV requirements is an alternative you may want to consider if you are unable to establish the market value of the cash flow that is proposed as collateral for a loan or group of loans. The MBL rule sets out the information a credit union must provide with a waiver request and how a regional director will process that request. 12 C.F.R. §§723.11-13.

Please contact Staff Attorney Frank Kressman or me with any questions or if we can be of further assistance.

Sincerely,

Sheila A. Albin
Associate General Counsel

GC/FSK:bhs
05-1219
cc: Region III