THE BRIDGE

PARTNERS IN COMMUNITY DEVELOPMENT

issue 6







Credit Unions United To Serve The Underserved

Federation

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PARTNERS IN COMMUNITY DEVELOPMENT

Federation

Credit Unions United To Serve The Underserved

The mission of the National Federation of Community Development Credit Unions is to help low- and moderate-income people and communities achieve financial independence through credit unions. We are a dynamic association of growth-oriented credit unions that have more than $39 billion in combined assets and provide safe and responsible financial services to 4.5 million Americans in urban, rural and reservation-based communities. Established in 1974, the Federation promotes financial inclusion by strengthening community development credit unions, also known as CDCUs, which specialize in serving the underserved. The Federation achieves its mission through:

INNOVATION

We develop new products that meet the needs of low-income wage earners; foster strategic partnerships with funders and community organizations; identify and promote best practices in financial services for LMI markets; and provide education and training to CDCUs.

INVESTMENTS

Our Community Development Investment Program invests in member CDCUs to strengthen their financial position and expand their impact on the low-income communities they serve. Federation investments help CDCUs offer responsible products that help consumers protect and build assets.

CAPACITY-BUILDING

Federation technical assistance, webinars, practical tools, guides, and consulting services support CDCUs at all stages of development; we help CDCUs to compete in their communities, grow their membership and strengthen their bottom line.

The National Federation of Community Development Credit Unions

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The Bridge is a magazine published by the National Federation of Community Development Credit Unions (Federation) intended as an educational resource highlighting best practices, insights and commentary to help credit unions better serve underserved and emerging markets.

President/Chief Executive Officer Cathie Mahon **Editor-in-Chief** Clarissa Ritter

Visit the Federation's website at **www.cdcu.coop/member-submission/** to submit photos of your credit union for use in future issues of The Bridge.

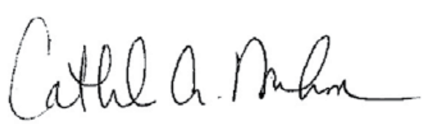
From the President's Desk

With all that credit union managers have to think about, it's easy to get lost in the everyday details of survival and lose sight of your most essential function: making good loans. For that reason, we decided to devote this issue of *The Bridge* to lending. Inside these pages you will find accounts of how community development credit unions are succeeding by lending to a diverse membership, offering innovative loan products and marrying technology and traditional practices.

Credit unions are reaching more people with responsible loan products than ever before. Nationally, loan growth has reached a ten year high and membership hovers around the 100 million mark. While there is much to celebrate, there are many more opportunities for credit unions to grow. Federation research presented at the 2015 GAC established that more than 2,000 credit unions have 100% of their branches in economically distressed CDFI Investment Areas.

Historically credit unions were formed to serve those individuals and small businesses that were unable to obtain credit elsewhere. That same purpose remains relevant today. CFED's 2015 Assets and Opportunity Scorecard reports that one in five households regularly relies on fringe financial services, such as payday loans, to meet their daily needs. American credit unions, with their rich history and experience in serving unserved markets, remain uniquely positioned to reach out to the estimated 88 million unbanked and underbanked in our country today.

As lenders to low-income consumers, our mission is to *manage* risk, not *minimize* it. We often hear that Federation members try to find a way to say "yes" when other lenders say "no". Today the tools exist to monitor and manage a diversified portfolio. For those who are competing for high-scoring members, there are thousands who will benefit from your credit union's safe, affordable and credit-building products while contributing to the bottom line. This issue of *The Bridge* will hopefully get you started thinking about how.



Cathie Mahon, President/CEO
Federation

SUCCESS WITH BORROW AND SAVE™

Borrow and Save™ Update

Combatting predatory lending is central to the Federation's mission of helping low- and moderate-income people achieve financial security through credit unions. Payday loans are predatory short term loans that charge exorbitant fees and interest rates that prevent financially vulnerable consumers from building assets. Only 17 states and the District of Columbia protect consumers against payday lending by prohibiting the loans or capping the interest rates they charge.

The need for an affordable alternative to payday loans led to the Federation's development of Borrow and Save™, a small dollar loan with a required savings component. Consumers borrow between $300 and $3,000, with 10 to 50 percent of the loan balance placed in restricted savings for the term of the loan. When the loan is repaid, borrowers have savings – and improved credit. Freedom First Credit Union in Roanoke, VA, among the first to test Borrow and Save™, has met with such consistent success with the product that it is now part of their Impact Banking Program. Since April 2014, 12 credit unions are offering Borrow and Save programs through Filene's Financial Services Incubator.

Perspectives from Four Borrow and Save™ Credit Unions

Credit unions that offer Borrow and Save™ have found that it is a low investment, revenue generating, productive entry point for borrowers who might not be eligible for other credit products. From April 2014 through the end of April 2015, the 12 credit unions participating in the Incubator closed over 2,430 Borrow and Save loans totaling over $2.4 MM, with borrowers saving almost $804,000 through their credit unions. Four of the credit unions in the program have shared their results and reflections on the program, including how Borrow and Save™ is improving savings behavior.

At *Southwest 66*, members like that a Borrow and Save™ loan is not based on their credit, but on their ability to pay back the loan. At *Seasons*, members report feeling more confident and feel they have more control of their loan payments; they especially appreciate the opportunity to build a positive payment history. At *Hope*, members like the longer repayment period, which allows them to take on more credit and build a stronger credit score – an opportunity they may not have had in the past. Sharing one particular success, *Peninsula* talks about a borrower named James:

"Peninsula CU was able to grant new member, James, a Borrow and Save™ loan in June 2014. He had good employment, but was in the beginning stages of divorce and found himself short on cash days before payday. James was also scheduled to head out of town for work and needed to pay the mortgage and provide food for his children before leaving. He came to Peninsula CU to find an alternative to a payday lender.

James has since paid off his Borrow and Save™ loan and thanked Peninsula CU for the help. In the time since taking out the Borrow and Save™ loan, he has been able to save $3000 for a down payment on a new car and has added $2000 to a savings account. And great news - he financed his new vehicle with Peninsula CU. James expressed his gratitude and is in a much better place in his life in part due to the assistance provided by PCU."

Like their members, the credit unions shared positive feedback with Borrow and Save™. For *Southwest 66*, the feature they most like is the required savings as it helps reinforce the importance of having a savings account. With *Seasons*, members are developing a dialogue with the credit union and building a relationship. They now see *Seasons* trying to set them up to be successful, despite their challenged credit. *Hope's* team has been particularly excited as Borrow and Save™ provides another tool for them to work with members who may not qualify for traditional loans. The loans at *Peninsula* have already had some repeat borrowers. All four credit unions share that they will continue with Borrow and Save™ after the pilot ends this year.

SUCCESS WITH BORROW AND SAVE™

continued...

Four Borrow and Save Credit Unions at a Glance:

Southwest 66 Credit Union in Odessa, Texas

- Total Assets: $77,531,000 | Membership: 10,300
- For Borrow and Save
    - Number of loans: 50
    - Total dollar amount of loans: $43,300
    - Average loan amount: $866
    - Total dollar amount put into savings: $10,825

Seasons Federal Credit Union in Middleton, Connecticut

- Total Assets: $123,958,000 | Membership: 16,200
- For Borrow and Save
    - Number of loans: 114
    - Total dollar amount of loans: $114,000
    - Average loan amount: $1,000
    - Total dollar amount put into savings: $47,000

Peninsula Federal Credit Union in Shelton, Washington

- Total Assets: $150,107,954 | Membership: 17,210
- For Borrow and Save
    - Number of loans: 52
    - Total dollar amount of loans: $38,842
    - Average loan amount: $746.96
    - Total dollar amount put into savings: $9,710.50

HOPE Credit Union in Jackson, Missouri

- Total Assets: $160,340,503 | Membership: 27,948
- For Borrow and Save
    - Number of loans: 488
    - Total dollar amount of loans: $421,450
    - Average loan amount: $863.63
    - Total dollar amount put into savings: $132,200

**All numbers as of December 31, 2014*

eMoneyPool – The Creditworthiness Tool and Bridge to Financial Inclusion

BY LUIS CERVERA

Our country is a melting pot, a place where great ideas and traditions are brought together from around the world. One of these great traditions has been in use for over 1,000 years and is known around the globe by over 200 names, including the Lending Circle or Money Pool.

Simply put, traditional lending circles are an agreement between members of a community who help each other borrow and save money in a disciplined manner to reach their financial goals. It provides access to capital to families with unexpected costs, to small business owners looking to upgrade equipment or replenish inventory, or for the average hardworking individual who desperately wants to take his family on that special vacation, but can't seem to find the money to make it happen.

Here's an example of how a money pool works: ten individuals form a pool, agreeing that each individual will contribute $100, for a total of $1,000. Each month, every individual contributes $100. One of the ten contributors gets the $1,000 for one month. The contributors each get the $1,000 once during the ten months of the pool.

Money pools succeed because they provide participants the perfect level of discipline that many of us require to meet our short-term financial goals. Amazingly, despite the traditional model's deficiencies, such as the hassle of running around to exchange money with your group, over *60 million Americans* are using money pools today.

Enter eMoneyPool.

eMoneyPool is an online platform, which has brought the lending circle into the 21st century, making it easier, safer and more efficient to participate. The exchanging of funds is done entirely through an ACH transaction from your active checking or savings account, making the process safe and hassle free.

Users can easily join together through their smartphone, PC or tablet with like-minded individuals from across the country, while eMoneyPool guarantees the entire process. As users participate and make payments on time, they begin to build trust within the online community, allowing users greater access and the ability to participate in larger pools.

An added benefit of eMoneyPool is the ability to track payment history. As an individual continues to make payments into a money pool, every payment is tracked, which begins to create a clearer picture of their financial habits. This "financial snapshot" is valuable to our lender partners, including many credit unions.

As users complete their money pools, eMoneyPool will refer them to our lender partners who accept our "Certificate of Completion", proof that an individual has made 10 payments on time. This then becomes an additional tool in the underwriting process, and may qualify eMoneyPool users for a traditional loan. eMoneyPool becomes a "Creditworthiness Tool" for its new and existing members. eMoneyPool has been proud to be partnering with Marisol Federal Credit Union in Phoenix, AZ since 2013 and offer its users the opportunity to begin building credit through MariSol's "Credit Builder Loan".

To further serve as a financial inclusion tool, specifically in regards to immigration reform, eMoneyPool has recently partnered with Emerge Financial Wellness, and in collaboration with the National Council of LaRaza, is offering our platform to immigrant families as a solution to help in financing their Deferred Action for Childhood Arrivals (DACA) and citizenship fees. Any individual looking to pay for these fees can participate with eMoneyPool, which by its inherent design, does not require an Individual Taxpayer Identification Number (ITIN), proof of income or proof of credit history. There is no such thing as not qualifying for a money pool. Our goal is to not only help immigrants meet their short-term DACA goals, but to help them take the next steps towards integrating into traditional financial products with our credit union lending partners.

Interested in becoming a lender partner?

Benefit from:

- Lead generation of current eMoneyPool users in your area ready to take the next step to a traditional loan
- Incentivizing your community to open new member accounts to participate with eMoneyPool
- Offering your current members a new product, which many will recognize, that provides a structured plan to help them meet their short-term financial goals
- The ability to offer your loan denials the option of participating in a money pool to prove their creditworthiness and then return with their money pool savings for a partially secured loan

Contact Luis Cervera, President and Co-Founder of eMoneyPool at luis@emoneypool.com or by calling 800-570-1947.

eMoneyPool

MyPath Credit Helps Young Adults Achieve Their Savings Goals

BY MARGARET LIBBY

A national non-profit based in San Francisco, MyPath powers youth potential and seeds economic mobility. MyPath's innovate approach engages low-income youth in banking, saving and credit-building by partnering with community development credit unions (CDCUs) to provide safe, quality financial products for youth and young adults. These savings and credit programs are then integrated into youth workforce programs, reaching youth as they earn their first paychecks. Combining access to products with in-person and online financial education, incentives and direct deposit, MyPath Savings has supported 85% of participants to achieve their savings goals, and MyPath Credit has resulted in 87% of participants improving their credit scores.

MyPath is currently piloting its newest program model, MyPath Credit, as part of the Financial Capability Partnership Initiative (FCPI) through the Federation and CFSI. This initiative fosters credit union and nonprofit service organization partnerships that integrate affordable credit union products into social and human service settings. MyPath Credit engages low-income young adults ages 18 - 24 in credit-building alongside saving, and unlocks their access to quality employment, college, housing, and loans. MyPath Credit incorporates Self-Help Federal Credit Union products and, with FCPI support, is being piloted at Year Up Bay Area, a nationally-recognized youth leadership and employment program.

MyPath Credit includes an introductory credit workshop, a credit-builder loan enrollment workshop, one-on-one financial coaching, and financial incentives. The results of the first year pilot have been remarkable: 226 youth received financial workshops, 83 received one-on-one financial coaching, and 60 youth opened a credit-builder loan and savings account. To date, 85.2% of participants saw improved FICO credit scores; every participant that started with no credit score is now scoring at 660+. Participants that started with low credit scores are improving on average by 32 points after about 6 months.

At the most recent FCPI convening, we heard directly from two alumni of the MyPath Credit program. These two 25 year-olds explained that MyPath Credit taught them about the "credit game" and helped them build credit for the first time; both young adults are the first in their families to have positive credit. One young woman shared that paying off her loan put her in a new position of financial independence, having recently moved into her own studio apartment. Having grown up homeless, she was deeply proud to have put a roof over her head without needing a co-signer on the lease. The other speaker focused on using her new positive credit to apply for a car loan from Self-Help Federal. As she put it, "Year Up and MyPath Credit gave me a fair shot at life." We already see MyPath Credit alumni continuing their relationships with Self-Help Federal after the program ends, applying for additional loans and

banking products, and referring their family and friends. The data we are gathering through the FCPI initiative will demonstrate the extent of the longevity of the relationships established through MyPath Credit.

MyPath Savings, our national savings and banking initiative, brings together local credit unions and youth employment programs to provide youth participants ages 14 - 24 with youth-owned savings and "spending" accounts, a blended model of innovative online and in-person financial education, and savings incentives. Last year 95% of participants opened savings accounts, and 85% met their personal MyPath Savings goal, on average saving 30% of their income. Our current credit union partners include Self-Help Federal in San Francisco/Bay area and United Federal Credit Union in Reno, NV.

This collaboration is a great opportunity for CDCUs to help low-income youth avoid predatory services while increasing visibility and marketing opportunities, and directly connecting younger members to appropriate products. We are currently looking for CDCU partners to expand our MyPath Savings Initiative to new cities. If you are interested in learning more about spreading financial capability among traditionally underserved youth and young adult populations, please contact Sabrina Kansara, Director of Strategy, at sabrina@MyPathUS.org.

Margaret Libby is the Executive Director of MyPath, which places low-income youth and young adults on a path to economic mobility by ensuring they have access to quality financial products, a working knowledge of the financial system, and a peer-based social support system that encourages personal goal-setting and accountability. When we do this, we position youth and young adults to achieve their full potential and seed upward economic mobility that will continue for generations to come.

my path

Notes from the Field:
CFLA Fellows Update

The CFLA program has completed its second year! Eleven new and emerging leaders finished the six-month program and are actively working in CDCUs throughout the US. Below find notes from the field written by the Fellows which gives an update on their progress.

The Federation is accepting 2015 applications for CFLA fellows and credit union sponsors through June 25, 2015. Thorough a generous grant from Citi Community Development we are able to continue the program for a third year. Look for additional information on our website: cdcu.coop/initiatives/credit-union-leadership-development/.

DeLise Simmons

It is indeed my pleasure to participate as a Fellow in the CFLA program. The week spent training in NYC was intense but well worth the trip. What I learned provided me with a better understanding of credit union operations and also of the importance of the credit union movement. ***Toledo Urban Federal Credit Union*** *is experiencing consistent growth in membership; one of my focus areas was to help educate our members and encourage them to take full advantage of all of the services that we offer. The weeklong training experience left me inspired to "step it up" and aggressively work to make our credit union the best in the city. The CEO and I worked together to prepare for our annual meeting and appreciation banquet as well as for the holiday loan promotions offered to our members. Our goal was to end 2014 on a high note! Thank you to the Federation for offering the CFLA program and for allowing me to serve as a Fellow.*

L to R: ***Suzette Cowell,*** *CEO of Toledo Urban Federal Credit Union, and* ***DeLise Simmons****, CFLA Fellow*

The Cooperative Federal team

Mary Beth Schwartzwalder

Training was a whirlwind of new information for me, especially during the first few days when we studied finance and learned just how hard it is to make decisions on lending. I spent most of my time at ***Cooperative Federal Credit Union*** *helping to roll out marketing and outreach on a few different initiatives, including Small & Micro Business Loans and Lunch and Learn opportunities. I also spent some time with our community development partners to support emerging entrepreneurs and small business owners. A small group of staff members and I attended short training sessions about "sales" and what that word means in Credit Unions. It seems that every day was a learning experience. I was especially excited to create a portfolio of member impact stories and further develop our field of membership.*

Notes from the Field: *CFLA Fellows Update*

continued...

Angie Baker

*It seems as if it was only yesterday when we all met in the Big Apple. I recall everyone sending selfies upon arrival and being so excited to be a part of this wonderful CFLA Fellowship. The week of training with Professors Allison and McQueen at the New School consisted of classes, workshops and case studies. All of these tools gave us a really great insight into Business Lending and much, much, more. During the six month Fellowship, continuous webinars were also instrumental in my day to day duties. As the Employee Development Trainer here at **Heart of Louisiana Credit Union,** I consistently use information and tools provided by the Federation.*

*L to R: **Cynthia Beauregard,** Heart of Louisiana CEO, **Angie Baker** and **Angela Clark,** CFLA Fellows*

Angela Clark

*The intense weeklong training provided me with the tools to begin my action plan. I have worked on finding ways to extend our membership to **Heart of Louisiana's** immigrant community. My first objective was to gather a list of the exact documentation needed to begin opening accounts. The webinars were useful in providing me with this information and more. It also helped me to understand how to continue to build that relationship and help our credit union to become a source of help for our growing immigrant community.*

*L to R: **Devin Cromwell,** CFLA Fellow, and **Patrick Adams,** CEO, St. Louis Community Credit Union*

Devin Cromwell

*My week of training in NYC was absolutely amazing. I was able to learn from the other fellows about good products and services they offer to their membership, and they were able to gather good ideas from what **St. Louis Community Credit Union** does to help our underbanked and unbanked population in St. Louis. I wanted to focus on some problem areas I learned about in training that may exist, like delinquency on loans, low loans to shares ratios, and more importantly building asset development for our membership by possibly implementing some of the good ideas from training. In addition, I wanted the credit union to be visible in the communities we are actually servicing and aid them more in their day to day life through partnerships with other nonprofit entities. As a Member Service Representative, I was able to have daily interactions with members; this is very helpful in determining the needs of the members, such as different loan types, and other ways to improve their day to day living. In addition to loans, I am also looking for ways to add more convenience to their funds by improving our mobile app and partnerships with other cooperatives to help members built assets.*

Veronica Miller

*After attending the CFLA training in New York City, I came back to **Holy Rosary Credit Union** with many ideas to help the credit union. I am both an AmeriCorps VISTA Fellow and a CFLA Fellow and helped our credit union change core processors in May while continuing to add new programs. We will be adding electronic signing soon! This program and a few more will help reach members who cannot come in during regular business hours. The blessing of working in the credit union movement is partnering with people and organizations moving toward the same goal: helping those in need.*

*L to R: **Carole Wight,** Holy Rosary Credit Union President, and **Veronica Miller,** CFLA Fellow*

Notes from the Field: *CFLA Fellows Update*

continued...

Candace White

Following an intensive week of CFLA training in NYC, I returned to ***Southern Chautauqua Federal Credit Union*** *and my new positon as the Director of Community Development. Southern Chautauqua FCU's vision is to be a resource to all residents of Chautauqua County, particularly those who are financially underserved. Therefore, my focus was community outreach and developing partnerships and programs which will best serve the needs of our current and potential members. My first responsibility was to select and mentor our new Kid's Credit Union Coordinator to ensure a smooth transition and the continuing success of our program. My CEO and I implemented the following services and initiatives at SCFCU: Green Path Financial Wellness; eMoneyPool; remote deposit capture and a student internship. I am looking forward to continuing my association with the Federation and sharing best practices (and some more laughs!) with my other CFLA fellows.*

L to R: ***John Felton,*** *Southern Chautauqua Federal Credit Union CEO, and* ***Candace White,*** *CFLA Fellow*

SOUTHERN CHAUTAUQUA FEDERAL CREDIT UNION

1199 SEIU Crew with ***Valentin Bonneau,*** *lower right*

Valetin Bonneau

As I was new to the credit union world, the weeklong training was essential for me to understand the basics of this industry. In fact, our class about loan analysis was the most important because I learned about the issues loan officers have to face when dealing with members. More importantly, listening to others' experience allowed me to picture the specific needs that credit union members have. I had an opportunity to institute a number of outreach and marketing campaigns that were successful for the ***1199 SEIU Federal Credit Union,*** *including the Holiday Loan program and the 75th Anniversary Sweepstakes. I created Facebook and Twitter accounts for 1199 SEIU as a free way to communicate our benefits and build the basis of our online presence. Social media fit right into our email marketing as scheduled emails and posts/tweets were linked to one another. Also, I assisted with the promotion of the Getting Ahead program (free financial counseling) among our members who had low credit scores. This program also offered a great opportunity for storytelling on our social media outlets.*

1199SEIU United Healthcare Workers East

More than a Score: Making a Difference Through Non-Prime Auto Lending

BY CHRISTOPHER MORRIS

Could you imagine if your members invited your staff to their weddings and other special events because your relationship with them is that strong? It's possible.

That's what happens to staff at Seasons Federal Credit Union in Middletown, Conn. Seasons FCU's Betsy Sommers, SVP, and Jeff Rindfleisch, Chief Lending Officer, explained to me recently that in 2011, the credit union moved to a more relationship-based model in working with their members. Decisions weren't made just on their credit score, but on listening and building relationships no matter what a member's score is. That's one reason why Seasons FCU chose to participate in the National Credit Union Foundation's Non-Prime Auto Lending pilot program. The pilot program, in partnership with the Filene Research Institute, kicked off in 2014, with 13 credit unions participating across the country.

Non-prime lending refers to the practice of making loans to borrowers with weak or no credit histories or limited payment capacity. NCUF's Non-Prime Auto Lending program helps lenders fairly price and manage non-prime auto loans and is based on NCUF's extensive work in the area, which includes previous grants and a free, comprehensive toolkit for credit unions. The program helps consumers gain access to reliable transportation which allows for increased access to jobs, housing, schools and activities. It also helps them avoid the costly pitfalls that come with buying from the corner buy-here-pay-here auto lots and other predatory lenders.

At Seasons FCU in Middletown, CT, they realized early on that in many cases most of the applicants for loans were simply denied by banks without being able to tell their unique story. Seasons FCU's staff listens to gain an understanding of the person's financial situation, and helps them find a car and payment that makes sense. This includes finding out their discretionary income (many people don't know what they can afford until you go through what their budget actually is), referring the members to reputable dealers in the community, and leveraging risk-based lending in a judgment free-environment.

This really has taken off for Seasons FCU for a few reasons. First, they've found that members have been extremely grateful as the credit union is serving members who aren't getting service elsewhere. Sometimes members will sob tears of joy that someone is actually listening to them, and then cry even more because Seasons FCU can help them get a loan. Second, because that relationship is so powerful, the members are much more likely not to miss a payment.

Seasons FCU not only lends this way, but they collect in a relationship-based manner as well. For example, they don't "dial for dollars" when collecting and if a member hasn't made a payment, Seasons calls them to find out what their situation is and ask what Seasons can do to help the member be successful. This could even mean finding another car in some cases. Seasons FCU appropriately changed the name of their collections department to "member solutions."

When asked why they do this type of lending, Season FCU's Rindfleisch noted, "This type of lending is part of the credit union philosophy and what we are charged to do as a cooperative. Everyone wants to reach the American dream and our job is to set members up for success."

Seasons FCU also focuses on credit counseling credit-challenged members to teach them how to rebuild their credit, which often leads to members getting a mortgage loan. Oftentimes, because these relationships are so powerful, the credit union and staff become a big part of members' lives. For instance, Rindfleisch was recently invited to a wedding where he didn't know anyone except for the bride and groom. In their wedding toast, the newlyweds thanked him personally for helping them buy their first house.

Christopher Morris is the Director of Communications at the National Credit Union Foundation; you can reach him at cmorris@ncuf.coop or (800) 356-9655 x4374.

The National Credit Union Foundation is the charitable arm of the US credit union movement and works as a catalyst to improve people's financial lives through credit unions. Through Foundation grants and programs, credit unions provide widespread financial education, create greater access to affordable financial services, and empower more consumers to save, build assets, and own homes. Donations to the Foundation enable credit unions to help their members reach life-changing goals and achieve financial freedom.

THE National Credit Union FOUNDATION

Small Business Lending... Why now?

BY WALTER MERKLE

Many credit unions have considered lending to small businesses… many already have! Lending to a self-employed member is a form of small business lending, even if we don't consider it as such. Members come in a variety of forms… those that are employed, receiving other forms of income, or who are self-employed. Here, we are speaking of those that are self-employed. Members may run their own business in a variety of ways… as a sole-proprietorship, in the form of a partnership, or in the form of a corporation… in whatever form they choose, the need here is not only to evaluate how well the member performs their "job," but also how well they run the business that provides their job! Clearly, if they are unable to run the business successfully, there may not be a job for them down the road!

In this day and age where credit unions are being required to be mindful of things such as growing their loan portfolio, mitigating against interest rate risk, concentration risk, etc., small business lending might be the answer, as long as it's done mindfully and performed by staff that have been well-trained in small business lending. While NCUA identifies a "Member Business Loan" at $50,000 or more individually or in aggregate to a business, prudency dictates that even smaller loans to small businesses be entertained, processed, underwritten and closed by a credit union staff member that has been trained and is experienced in small business lending.

So where to start? Perhaps the best way to start is to partner with a CUSO that can process loans while you gain experience in small business lending. Once you gain experience, you might want to start by making fixed asset loans, e.g. for the purchase of vehicles and other fixed assets like machinery and equipment. I would caution against starting off by financing commercial real estate or by providing working capital financing. There is additional expertise that is required for both types of financing. I would also recommend that a credit union considering starting a small business lending program start off small, limiting the amount of loan capital it will invest and by clearly articulating its "Program Expectations," e.g. anticipated volume, staff requirement, yield, losses, etc. Only then can a credit union monitor their performance against their anticipated expectations.

At the end of the day, lending is lending, whether a credit union lends to an employed individual or a self-employed individual you still need to consider the basic aspects, (the C's) of credit -- membership standing, repayment ability, repayment willingness, a secondary source of repayment (collateral). In the case of self-employed borrowers you also need to consider management's ability to successfully run the business so that there is repayment ability going forward. You will also want to consider conditions that might adversely affect the business as well as the extent to which the owner has invested in the business. Business lenders feel more comfortable when the business owner has "some skin in the game!"

As to "underwriting" a business applicant, repayment ability is typically measured by a business's debt-service-coverage ratio which is their cash flow (net income + depreciation + amortization) to debt service obligations (monthly loan payments)… it's basically the inverse of the debt-to-income ratio…. A debt service coverage ratio of 1.25x or greater is sought. As to evaluating repayment willingness, in most cases it's based on the credit history of the "principals" of the business, those that own 20% of more of the business. In the case of a sole proprietorship, that would be the owner, in the case of a partnership, that would be the partners, in the case of a corporation that would be the folks that own 20% or more of the stock of the company.

Small business lending can be done successfully and profitably and can be a great addition to your product offering if done mindfully and prudently! Best wishes!

Walter Merkle is a highly experienced credit union executive that has an extensive lending background and currently specializes in loan portfolio and financial performance management. Walter is the Executive Vice President at Northwest Georgia Credit Union a $70 million credit union in Rome, Georgia.

NORTHWESTGEORGIA CREDIT UNION

Lending To Less-Than-Prime Borrowers

BY DENNIS CHILD

Some argue that as the economy strengthens consumers and financial institutions are doing better. That is not necessarily true. Consider the following:

- Credit unions, particularly small ones, still struggle to increase their loan portfolios and their profitability
- Burned by the recession, many financial institutions still avoid loaning to borrowers with low credit scores and find themselves in tough competition for prime borrowers
- There are many consumers with less-than-prime credit ratings who are unable to borrow at reasonable rates or terms that would benefit from loans priced according to risk
- Many consumers with less-than-prime credit ratings are victims of the "Great Recession" who had stellar credit previously and are still struggling to re-establish their credit and obtain loans to purchase large ticket items long overdue for replacement

In light of the above observations, it can be argued there is much to be gained by credit unions by establishing a validated Concentration Risk policy, utilizing stochastically derived, randomly determined Risk Based Loan Pricing and extending loans to less-than-prime borrowers.

Credit unions that serve less than prime members enjoy political, public relations, and bottom line benefits. When priced and managed correctly, making loans to less-than-prime consumers can raise ROAA by as much as 30 basis points. Many of these consumers had good credit at one time, and given borrowing opportunities will return to prime status. Less than prime borrowers also tend to be more loyal to their financial institutions and use more services compared to price-shopping prime borrowers. Competition for prime borrowers can be fierce and can lead to price wars and lower profitability for your credit union.

When credit unions serve less-than-prime members they are in line with the 1995 NCUA-issued Guidance Letter -174 which states "credit unions should engage in risk-based lending, not as a means of re-pricing existing balance sheets, but as a tool to reach out to the underserved and take risk that might otherwise be avoided." A credit union that lends to less-than-prime borrowers that uses risk-based loan pricing usually experiences increases to their member base, grows their loan portfolios and sees improvements in profitability. Regulators are supportive of credit unions that use statistically validated models, including risk based loan pricing, and are generally pleased with the results.

As pointed out earlier, Risk Based lending should be pursued only under the most carefully managed conditions. The use of stochastically derived and statistically validated Risk Based Loan Pricing models are imperative. A Risk Based Loan Pricing model should consider all costs inherent in a credit union's lending process (unique to the particular credit union - not national statistics) including:

- Cost of funds
- Loan operations (using Activity Based Costing)
- Collections
- Charge-offs

A viable Risk Based Loan Pricing model should also:

- provide regular statistically founded validations (back testing) with upgrades to the pricing structure as appropriate
- build in profit margins according to management's strategic planning
- provide interactive "what if" scenarios, allowing managers to observe real-time effects on revenues under different proposed changes to pricing
- provide reports and pricing recommendations broken out by loan terms, loan types, credit grades, etc.

Extending credit under carefully managed conditions to less-than-prime borrowers benefits the industry, individual credit unions, and consumers.

Dennis Child is Marketing Director for TCT Risk Solutions, LLC and a 40 year credit union CEO veteran. TCT is a partner with the National Federation of Community Development Credit Unions. Dr. Randy Thompson, CEO of TCT, designs his training and management tools using empirically based, statistically validated methods and research. TCT has provided services to credit union and bank professionals for 25 years. TCT's clientele includes credit unions, credit union trade associations, and federal and state regulatory agencies. TCT is based in Boise, Idaho and can be reached at (208) 939-8366 or www.tctrisk.com

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Financial Inclusion for Immigrant Consumers

In early 2015, the National Federation of Community Development Credit Unions launched Financial Inclusion for Immigrant Consumers, a national campaign to link unbanked and underbanked immigrants in the US with credit union products and services for citizenship and legalization. Financial Inclusion Roundtables have been held in Los Angeles, New York, Dallas and Tampa Bay. Many thanks to Coopera and NLCUP, the Network of Latino Credit Unions and Professionals, along with the Federation members, partners, supporters and sponsors that have made these convenings possible. For programs, speakers, presentations, blog postings and photos visit www.cdcu.coop/initiatives/serving-underserved-markets/immigrants/financial-inclusion-for-immigrant-consumers-roundtables/

Los Angeles Roundtable: Pictured left to right are Lucia Moreno, Pablo DeFilippi, George Poitou, Miriam De Dios, Gary Perez, Councilman Gil Cedillo, Cathie Mahon, Carl Stewart, Leticia Mata, Larry Palochik

NYC Roundtable: Pictured left to right are Pablo DeFilippi, Francisco de la Torre, John Lewis, Ambassador Sandra Fuentes-Berain, Monsignor K. Sullivan

Dallas Roundtable: Pictured left to right are Maria Martinez, Oscar Bazoberry, Dick Ensweiler, José Octavio Tripp, Francisco de la Torre, Pablo DeFilippi, Edurne Pineda Ayerbe, Ursula Rojas, Jorge Jimenez, Matt Davies

Tampa Bay Roundtable: Pictured left to right are Sherod Halliburton, Lindsay Daniels and Roberto Nicolas Vazquez

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