**LOAN PARTICIPATION POLICY**

# POLICY

It is the policy of the credit union to participate in loans to credit union members jointly with eligible organizations up to a funding percentage not to exceed a 90% undivided interest of the total loan(s).

# DEFINITIONS

1. “Participation loan” means a loan where one or more eligible organizations participate pursuant to a written agreement with the originating lender.
2. “Eligible organizations” means a credit union, credit union organization, financial institution, or financial organization.
3. “Originating lender” means the participant with which the member contracts.

# GENERAL CONSIDERATIONS

1. The originating credit union will comply with applicable state or federal lending regulations.
2. If the total interest in a participation loan combined with prior participation loan purchases and other indebtedness owing to the credit union exceeds 10% of total assets, management will complete a credit concentration study.
3. A written master participation agreement will be properly executed by

 on behalf of the credit union. The master agreement will include provisions for identifying the participation loan or loans prior to their sale.

1. the credit union will screen each new originator offering loan participation pools.
2. Upon approval of a loan participation program the board of directors will adopt the program originator’s policies, procedures, and guidelines as its own loan policy, either directly or by reference.
3. Management will conduct periodic audits and reviews with loan participation originators to verify the accounting process, separation of duties for internal control, and maintenance of proper contingency plans.
4. Management will consider the maturity of loans in the participation portfolio to control the risk of loss from increases in the level of interest rates, defaults, and forced sale of loans.
5. There are two distinct types of loan participation agreements which may be entered into by the credit union:
	1. Loans purchased with recourse to the selling organization.
	2. Loans purchased without recourse to the selling organization.

Each type demands a unique due diligence procedure as outlined in the due diligence section below.

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# DUE DILIGENCE PROCEDURES

The due diligence examination will consist of the following:

# Due diligence procedures for selection and approval of originating organization:

* A review of the past twenty-four months financial performance will be performed, including: Annual Reports

CPA audits

Internal financial statements

* A financial analysis of the originator will be performed to determine trending analysis in the areas of capital, earnings, delinquency and loan loss ratios.

Minimal Data for Analysis: Equity Capital/Total Assets

* + Net Income and Cash Flow Statements
	+ Delinquent Loans/Total Loans
	+ Repossessions/Originations (if material)
	+ Net Charge-Offs/Average Loans
* A review of loan policies and delinquency and collection procedures.
* References will be requested and verified. Prior loan participation experience is preferred.
* Visit originator’s operations to review the concept of the business and verify that operating systems, policies, and procedures support the business model and are consistent with this policy.
	+ Organization is capable of segregating the loans to be sold on their computer system
	+ Documentation required: A file or printout of segregated loan portfolio.
	+ The form and substance of the monthly and other periodic reports will be accurate and provide adequate information for accounting and delinquency reporting purposes.
* Evaluate the financial management and risk factors associated with the program to ensure they are consistent with this policy, including:
	+ Financial responsibility of the originator supporting the program.
	+ Known adverse information regarding the originator appearing in the press will be reported by management to the board of directors.
	+ Risk of default and estimated risk exposure should default occur.
	+ Special features that may mitigate credit union’s exposure.
	+ Credit enhancement features that are part of the program.

All documentation will be filed with the master loan participation agreement and will be retained until the loan participation purchased has been paid in full, returned to the originator, or charged-off.

# Due diligence procedures for RECOURSE AND NON-RECOURSE loan purchases:

1. Obtain a copy of the loan underwriting policy and review to establish that the policy is reasonable and meets the requirements of the credit union.
2. The selling organization’s collection policy and actual procedures are appropriate and effective for the type of loans being sold.
	* Review collection policies and procedures
	* Interview personnel regarding implementation of these procedures.
3. The seller’s operational procedures are adequate to properly service the loans.
	* Review payment-processing procedures.
4. The projected net yield for the pool of loans being considered has been calculated.
5. The projected net yield will be compared to net yields available on other investments to determine if the compensation is adequate for the risk assumed.

# Additional due diligence procedures for NON-RECOURSE loan purchases:

1. The loan underwriting practices of the seller is compliant with their internal policies.
	* Review a random sample of loans from the proposed participation pool.
2. The historical loss ratio for the pool of loans being considered for purchase will be calculated. If the pool does not have an historical loss ratio the loss ratio for similar loans held by the originator may be substituted.
3. Minimum acceptable underwriting standards for the type of loans being purchased may include:
	* Type of loans in the pool
	* Securing titles
	* Insurance for collateral
	* Debt ratio limitations
	* Loan terms
	* Credit report standards

# STANDARDS FOR THE ORGINATING LENDER

An originating lender will:

1. Underwrite loans based on the lending policy and guidelines provided to the credit union and agrees to send updates to the lending policy and guidelines as they are made.
2. Only make loans to individuals eligible for membership in one of the participating credit unions.
3. Retain an interest of at least 10 percent of the face amount of each loan. If the originating lender is not the organization selling the loans the organization selling the loans will retain a minimum 10% interest in each loan.
4. Retain the original loan documents or legal substitute loan documents.
5. Require the use of the same underwriting standards and collections standards for participation loans as for loans that are not being sold.

# STANDARDS FOR THE PARTICIPATING CREDIT UNION

As a participating lender, the credit union will:

1. Have a lending or participation policy in place that sets forth the loan underwriting standards for the particular type of loans prior to entering into a participation agreement.
2. Retain the original or a copy of the written participation loan agreement and a schedule of the loans covered by the agreement.
3. Obtain the approval of the board of directors or delegated management official for the disbursement of proceeds to the seller.
4. When the loan type is outside of the general business practices of the credit union, an experienced underwriter with expertise in the field identified will be used as a consultant.
5. Ensure the purchase complies with all regulatory requirements to the same extent as if the purchasing federally insured credit union had originated the loan, including, for example, the loans-to-one-borrower provisions in NCUA and state requirements for consumer and member business loans.

# ON-GOING DUE DILIGENCE PROCESS

Financial Review: At lease semi-annually, obtain and review financial information provided by the originator. Obtain certified, audited, or regulatory financial information when available.

Participation Status: Review actual program performance against this policy and overall goals in order to ensure the program is meeting expectations.

# UNDERWRITING PROCEDURES

Underwriting procedures will vary for each type of loan participation based upon loan type and whether portfolio is with or without recourse to selling organization.

# For Portfolios with recourse, the following minimum information will be analyzed:

* 1. Most Recent Audited Financials
	2. NCUA 5300 or FPR and FPR ratios reports (if applicable)
	3. Most recent internal financial statements
	4. Loan Policy
	5. Delinquency and Collection Procedures

# For portfolios without recourse the following will be reviewed on a random sample of loans:

**Automobile Loan Participation**

* + 1. Loan application
		2. Evaluate credit report
		3. Examine proof of income and ability to pay
		4. Verify collateral value
		5. Recalculate loan to value
		6. Verify that the terms of the loan are within the originator’s loan policy limits

# Mortgage Loans

1. Review loan application
2. Evaluate credit report
3. Examine proof of income and ability to pay
4. Verify LTV and appraisal
5. Verify that the terms of the loan are within originator’s loan policy limits

# LOAN ORIGINATION AND ADMINSTRATION

Credit guidelines and loan origination will be completed as follows:

* Originator prepares the loan documents that comply with applicable state and federal regulations.
* Loan documents will be fully completed and will result in valid and binding obligation of all borrowers to pay the loan according its term and with a valid and enforceable first lien on the collateral.
* Originator will verify the borrower has appropriate insurance in the full amount of the collateral as shown on the purchase contracts. Insurance will be payable to the originator, or the credit union or both as applicable.
* Originator will maintain in its possession all documents and records necessary for evidencing, securing, and servicing the loan. Originator will provide access to these documents at any reasonable time.

# ANNUAL REVIEW

This policy is subject to annual review by the Board of Directors.

# Approved by the Board:

**Date:**