



# BULLETIN

## Colorado Division of Financial Services

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Colorado  
Department  
of  
Regulatory  
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**Issued to: State-Chartered Credit Unions**

**Subject: Purchasing Loans and Loan Participations**

**Date Issued: May 8, 2003**

On December 20, 2002, this office issued a regulatory bulletin regarding purchased construction loans. Please refer specifically to that bulletin for additional detail, but our conclusion was that some credit unions experiencing problems with purchased construction loans or participation interests were relying excessively on the originating mortgage company for proper underwriting and loan administration. Therefore, we advised credit unions not to engage in such activities at all, if they did not possess the expertise to thoroughly analyze the underwriting of higher-risk loans or participation interests and closely monitor loan administration.

As we conduct examinations, we continue to see problems with purchased loans and loan participation interests of varying types, including residential construction, commercial real estate and other business lending. Economic conditions regionally and nationally are poor, and the combination of economic forces and deficiencies in underwriting and administering loans are adversely affecting asset quality and earnings in some credit unions. Therefore, it is necessary to more specifically set forth the Division's expectations of state-chartered credit unions that wish to engage in such forms of lending:

1. The credit union first must have sufficient written policies and procedures to properly guide its purchases of loans and participation interests.
2. The credit union must have personnel on staff (or by contract with a third party) with demonstrated expertise in analyzing, underwriting and recommending credit decisions for the particular type of lending.
3. The credit union's board of directors and top management must become sufficiently knowledgeable of the particular type of lending to be able to provide appropriate oversight.
4. Finally, the credit union must maintain appropriate file documentation to support its loan underwriting and the proper administration of the loan.

What is appropriate file documentation? Assuming that whole loan and loan participation purchases will be without recourse to the originator, the Division's expectation is that state-chartered credit unions will have a copy of the complete loan file on premises. In addition, the purchasing credit union should have a document check list and loan approval sheet that includes approval signatures and basic underwriting data such as the debt ratio and loan-to-value ratio. Purchasing loans and participation interests can be a viable and prudent business strategy, but in the final analysis, the risk of loss to the credit union and its members is at least the same as with originated loans. Therefore, management has a responsibility to demonstrate the validity, quality and compliance of a purchased loan asset just as it does with a loan originated in-house, and accordingly, Division examiners will have similar expectations in terms of documentation.

The Division's position in this matter stems from the premise that a credit union's board of directors and top management can delegate the authority, but not the ultimate responsibility, for the credits they are putting on the books.

This bulletin is not intended to provide comprehensive guidance regarding purchases of whole loans and participation interests. It is more narrowly focused on the Division's views on credit union management responsibilities and documentation requirements. Should you have questions, please do not hesitate to contact your assigned Division examiner or this office.