

Participation Considerations

There is no doubt that business lending is one of the hot button issues for 2004. The NCUA, the US Small Business Administration and all of the trade organizations have weighed in with ideas, opinions and rulings designed to help Credit Unions down the path to offering small business loans. But, business lending is not a simple process, it takes careful planning and expertise. Consequently, there are some credit unions that are buying participations as a perceived quick way to benefit from the business lending market, without originating.

If this is the route you choose, beware! Participations can be a useful tool, but there are traps... The first pitfall to consider is credit analysis; it can be stated as simply as this: don't make loans you don't understand. If you wouldn't feel comfortable originating a loan for any reason other than size, why are you participating in it? You need to not only understand the analysis of the business as presented to you, but also the underlying credit, and the lead lender's assumptions. In addition, you need to have faith in the originating lender's capabilities. Do they have the skills necessary to properly evaluate and service this loan?

The second hurdle to consider is risk. If your capital is tied up in one or two large participations, you stand at a much greater risk than if that capital is spread out across a number of loans. Which is more desirable, two \$500,000 participations, or ten \$100,000 originations?

Most importantly, there is the issue of member service. Are you offering your members any greater service by purchasing participations in lieu of actually making small business loans? No--one of the best reasons to begin business lending is to support the growth of your community and your members, and buying participations in some other state or area does neither.

Commercial loan participations can be an excellent addition to your credit union's activities, but they are simply not an acceptable substitute for serving your members.