



**12<sup>th</sup> Regional Meeting and Regional  
Youth Workshop on CU Marketing Across  
Generation:**

**“Youth of today leaders of today “  
Sept 15 to 18, 2011**

**Malaysia**



**ASSOCIATION OF  
ASIAN CONFEDERATION OF CREDIT UNIONS**

## **1) Introduction**

The deregulation of financial market is creating more competition to cooperative financial institution. Today, players could expect short-lived financial services in the market. All players have to be innovative and creative simply because of the consumerism behavior of the market.

Financial service is the main product of the credit union and these services should be delivered in accordance of what members' want. Any kind of service should be tailored made. Today, Board of Directors cannot assume on members' need. It has to be packaged according to the needs of the different segment of the market. Further, credit union cannot be relevant if it has not addressed the needs of its members. If the services were what the market want, thus there would be sustained growth and viability of the credit union.

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In reality the products and services of the credit union are still very traditional. It has failed to position itself in the market as one of the choices for financial services. It is still seen as cheap credit and savings as collateral for loans. In this situation, credit unions are seen as credit institution.

The youth market segment is a strategic area in developing product. In fact, credit union membership is 45 and above and it is really ageing. Credit unions still need to exert its effort in bringing youth as members and leaders as well. Youth is the largest market segment of the credit union market. By bringing the youth as users of credit union services, it would be able to teach young people the value of savings at early age.

Credit Unions/cooperatives are increasingly discovering the value of youth as members, leaders and be part of the management. ACCU program has also been experiencing increased communication with youth through its member federation/league and in the ACCU newsletter. Since 1992, ACCU initiates and implements program to market the CU to the next generation. The youth, which comprise of the 35% of the population in Asia, is a strategic market to increase the membership in credit unions. ACCU introduced specially designed range of products that will attract youth to patronize.

This workshop intends to review the achievement of the ACCU's member organization in promoting credit unions to youth market segment, identify the challenges, introduce enhancement to products and services and improve marketing strategies to increase youth using the services of the credit unions.

## **2. Objectives**

The overall objective of the workshop is to assess the impact on marketing credit unions to youth and to innovate product and services for youth tailored on their taste and needs.

Specifically, the objectives of the meeting are as follows:

1. To share the experiences and achievement of the marketing and promotional program of youth.

2. To reassess present products and services of CUs for youth market.
3. Develop strategies and technical plan to reach youth market demand.

### 3. Participants

The workshop is open to all ACCU member organizations with a special focused program on marketing to youth. However, it is more appropriate to send the person in-Charge in product development at the federation level and the President of the National Youth Task Force Committee. (Age limit is 18 to 29) Participants should have a thorough understanding of credit union operation and the Youth issue in the country. Participant must have communication ability in English.

### 4. Organization of the Workshop

The workshop will be organized in Malaysia on September 15-28, 2011. The recommendation and the result of the meeting will be presented to the CEOs Advisory Committee. The participants will have an opportunity to attend the Asian Credit Forum 2011 on September 19 to 22, 2011

#### Youth Workshop on CU Marketing Across Generation:

<b>Thursday Sunday, September 15, 2011</b>	
15:00 – 17:00 hrs.	Arrival and Registration
<b>Monday, September 16, 2011</b>	
08:30 – 10:00	Joint Opening Session (with other workshop groups – Youth, Women and CEOs)
10:00 – 10:30	AM Break
10:30 – 11:00	Introductions and Orientation
11:00 - 12:00	Group Work: Discovering the Youth Market? Why Investing in Young Members?
12:00 - 13:00	Lunch
13:00 - 14.00	Review of the policy on Products and Services for Youth
14:00 – 15:00	Country Presentations
15:00 – 15:30	PM Break
15:30 – 17:00	Country Presentations
<b>Friday September 17, 2011</b>	
08:30 – 10:00	Management Team Report Building Marketing Relationships with Young Members “How to overcome commercialization against values of savings and Thrift: Youth Perspective”
10:00 – 10:30	AM Break
10:30 – 12:00	Programs for Children and teenagers
12:00- 13:30	Lunch

13:30 - 15.30	Tailoring Services for Children and Teenagers
15:00 – 15:00	PM Break
15:30 – 17:00	Internet Services for the Wired Generation
<b>Saturday , September 18, 2011</b>	
08:30 – 10:00	Management Team Report , Young Adult program and predicts
10:00- 10:30	AM Break
10:30 – 11:00	The Next Generation of Youth Marketing
11:00 – 12:00	Preparation of Recommendation on the Continuing Professional Development of Leaders and Executives of Credit Unions (to the Joint Closing Program)
12:00 – 13:30	Lunch Break
13:30 – 15:00	Action Plan and Evaluation
15:00 – 15:30	PM Break
15:30 – 17:00	Presentation of Recommendations (Joint – CEOs, Youth, and Women)

**Day 4                      September 19 , 2011 Monday y Field visit:**

08.30 – 21.30    The participants of the Open Forum and Workshops will be divided into 10 groups and arrange field visit.

**Day 5                      September 20 2011 Tuesday 08.30 – 22.30**

08.30 – 17.30                      Asian Credit unions Forum 2011

**Day 6                      September 21 2011 Wednesday 08.30 – 22.30**

08.30 – 17.30                      Asian Credit unions Forum 2011

**Day 7                      September 23 ,2011 Thursday**

Departure Colombo

**INTRODUCTION:**

The Asian credit union movement as a whole faces major challenges in its efforts to reposition and professionalize. As identified by ACCU and its members, some of these challenges include:

- A social welfare image of credit unions in the market place - e.g., set up only for poor people with limited means.
- A lack of an enabling legislative and regulatory environment that could impose prudent operating standards on credit unions.
- A heavy reliance on volunteer management, rather than employment of professional financial managers.
- A highly competitive and rapidly evolving financial sector.

Repositioning the credit union movement in Asia is a long-term endeavor. Recognizing the constraints faced by ACCU, in terms of financial and human resources, the interventions that ACCU undertakes must be strategic and designed to create sustainable mechanisms, whereby national federations can build on the fundamentals of CU systems, development and strengthening, thereby increasing the competitiveness of established credit unions.

Based on 40 years experience, ACCU deemed it necessary to provide tool or system as part of the training or technical assistance to members. ACCU began introducing the credit union business solutions in 2000 through its member organizations' training or technical department who in turn transfer the technology to credit unions on a fee for service basis.

The 16 Credit Union Business Solutions developed by ACCU are responses to the current and perceived challenges faced by credit unions. The business solutions are practical tools credit unions can adopt to build the institution, create lasting impact to members' well-being, and equip human resources without losing grip of our differentiation –credit union principles and values.

## **OBJECTIVES:**

The HRD workshop serves as platform to develop and innovation and training resources. At the end of the workshop, the participants are able to:

Thus, the Training is to build the capacity of Leaders , officers and Managers of Credit union on credit management and delinquency. This training is covered credit Management delinquency Monitoring tools.

After the workshop, the partner coops will be able to:

- Adopt the policy forceful implementation and monitoring of the prudential standards, policies and financial disciplines on a monthly basis
- Adopt policies on Credit Management
- Agree to launch a delinquency management tools
- Adopt regular monthly reporting format for on delinquency

## **WORKSHOP TOPICS**

### **1. Credit Management**

- Review of the General Lending Policies and Capacity Based Lending

- Credit Investigation Procedures
  - Loan Characteristics and Loan Documentation
  - Loan Process
- 2 **Delinquency Control**
- Collection Process (Review)
  - Loans Portfolio Review and Control
  - Loan Legal Documents
  - Delinquency control

## **PARTICIPANTS:**

The workshop will be attended by Officer/s in-charge of HRD/Training of ACCU member organizations, who automatically forms part of ACCU Human Resource Development Committee. The committee provides input to ACCU on issues and strategies required to develop the human resource of credit unions.

The participants will have an opportunity discuss, share the experience and analyze the effectiveness of the present training programs of the federation in response to challenges faced by credit unions.

The participants will be attending the field visit and Asian Credit Union Forum 2011.

## **METHODOLOGY:**

The workshop shares and exchanges ideas and experiences on training and human resources development. Thus, a highly interactive participatory approach will be adopted. An experienced resource person will facilitate the workshop.

## **DATE AND VENUE:**

The workshop will be organized on September 16-18, 2011 in Malaysia.

### **“Credit Management and Delinquency Control” September 16 to 18 , 2011 Daily Schedule**

### **Tentative Daily Schedule**

*Resource Person:*      *Specialist* – Ms. Daisybelle M. Cabal, Finance and Management Analyst of NATCCO

<b>Thursday September 15, 2011</b>	
15:00 – 17:00 hrs.	Arrival and Registration
<b>Friday , September 16, 2011</b>	
08:30 – 10:00	Joint Opening Session (with other workshop groups – Youth, Women and CEOs)
10:00 – 10:30	AM Break
10:30 – 11:00	Introductions and Orientation

11:00 - 12:00	<b>Credit Management</b> <b>1.ELIGIBILITY</b> 2.ASSESSMENT 2.Deferred/Rejected loans 3 DELEGATION OF APPROVAL AUTHORITY 3.1Loans to Directors, Sub-Committee Members and Staff of Credit Union 3.2 Delegations 4 UNSECURED LOANS 4.1 Maximum limit 4.2 General conditions 5.5 Preparation/Registration of security documents
12:00 - 13:00	Lunch
13:00 - 14:00	5.SECURED LOANS 5.1 Maximum limit 5.2 General conditions 5.3 Insurance 5.4 Valuations of Securities ;Real estate ;Motor vehicles; Life Policies; Chattel Security Over Other Than Motor Vehicles. Caravans and Boats
14:00 – 15:00	INTEREST RATES 8. FUNDING
15:00 – 15:30	PM Break
15:30 – 17:00	9. LINE OF CREDIT LOANS 10. GENERAL
<b>Saturday September 17, 2011</b>	
08:30 – 10:00	2 LOAN CHARACTERISTICS 1Term and Modes of Repayment 2 Acceptable Payments 2.1. Checks 2.2. Payment in Kind or Service 2.3. Payment of Loan Proceeds 2.4. Interest Rates 2.5. Service Fee 2.6. Penalty 2.7. Delinquent Loans 3 LOAN PROCESS 1. Loan Application Stage 2. Credit Investigation 3. Loan Evaluation 4. Collateral Appraisal 5. Loan Release 6. Loan Monitoring 1.
10:00 – 10:30	AM Break
10:30 – 12:00	4 LOAN DOCUMENTATION 2. General Conditions Documents before Loan Approval

	Documents after the Approval
12:00- 13:30	Lunch
13:30 - 15.30	5 CREDIT INVESTIGATION 1. Field Investigation Factors to be checked
15:00 – 15:00	PM Break
15:30 – 17:00	6 CHARGE-OFF POLICY 1. Process 2. Requirements 3. Post-Charge-Off Activity Other Procedures Settling Charge-off Account Denial of Services
<b>Sunday , September 18, 2011</b>	
08:30 – 10:00	7 FORECLOSURE POLICY 1 Procedures 2 Post Foreclosure Process 3 Alternative to Foreclosure 4 Disposal of Foreclosed Properties Report 1: Daily/Weekly Collection Monitoring Report <b>Report 2: Aging of</b>
10:00- 10:30	AM Break
10:30 – 11:00	<b>Review of the credit management and Delinquency Management</b>
11:00 – 12:00	Preparation of Recommendation on the Continuing Professional Development of Leaders and Executives of Credit Unions (to the Joint Closing Program)
12:00 – 13:30	Lunch Break
13:30 – 15:00	Action Plan and Evaluation
15:00 – 15:30	PM Break
15:30 – 17:00	Presentation of Recommendations (Joint – CEOs, Youth, and Women)



## **Trainers Note and session guide for the Credit Management and Delinquency Control**

### **TYPES OF CREDIT (25 minutes)**

There are two types of credit their credit union might offer to members:

closed-end credit and open-end credit.

#### **Closed-end credit**

This is a one-time loan given to the member. It is finite.

The exact amount of money that will be loaned is determined from the very start.

This is the amount that is repaid, with interest.

If members want to borrow additional money, they must apply for a new loan by filling out a new application.

This is also known as *installment credit* because the loan is repaid in equal installments and is due on specified dates within the loan contract.

Installments can be either principal and interest payments, principal only repayments, interest only repayments, or balloon payments which is one payment at the end of the loan term. The type installment for the loan is determined within the loan contract.

Typical examples of closed-end credit are purchases for seed for planting, feed for livestock and other loans to purchase a one-time item.

#### **Line of credit**

This is a credit limit established for the member up to a pre-approved amount and up to a specified time period.

As long as the member doesn't go over the limit, he is free to borrow against this limit at any time and in any amount during the term of the line of credit loan.

Line of credit must meet two conditions.

**First**, the credit union must understand that the member will have repeated transactions with this plan.

**Second**, it is understood that, as the member repays the amounts he borrows, the available credit will be replenished up to the limit that was originally established.

Advantages and disadvantages comparing Close End Loans to Credit Lines.

Advantages of Close End Loans:

Easier for Credit Union to Manage Liquidity-one time loan disbursement, and no further need to monitor cash needs based on additional loan advancements as is needed with Credit Lines.

**Disadvantage of Close End Loans:**

Members may not need the whole loan amount at one time.

Advantage of Open End Loans:

Easier for member to manage cash flow; loan advances are taken when needed based on loan purpose.

**Disadvantage of Open End Loans:** More difficult for credit union to manage liquidity or cash needs of credit union. Credit Union must be prepared to be able to disburse credit to member on a periodic basis. Advantage of Credit Lines:

**For the Member:** Credit Lines are more advantageous to members when they do not need the whole loan amount advanced to them at one time. With Credit Lines members are able to determine when the need for cash exists and notify the credit union when their disbursements are to take place.

**For the Credit Union:** Credit Lines are a popular service that credit unions may offer their members to assist them with their financial needs. It assists the credit union by smaller loan amounts being disbursed to the member with more manageable repayments, which results in the lowering of loan non repayment by the member.

**Maturity**

The maturity date is the date on which the loan will be fully paid.

This date depends on the purpose of loan, the amount, and the collateral, if any.

For example, a member has taken out a loan to purchase seeds to plant tomatoes. The maturity date will be matched against the harvest date of the tomatoes. This will ensure the farmer has the cash flow once selling the tomatoes to pay off the loan at the credit union. (Monthly or Quarterly payments are matched against the farmers cash flow for interim payments prior to loan maturity date.)

**Terms of repayment**

These are the conditions that apply to loan repayment.

The most common condition is that the loan be paid in monthly installments.

However, a condition of an agricultural loan might be quarterly payments (when the crops are paid for).

It must be stressed that regular payments from the member is the most beneficial, both to the credit union and to the member.

**Benefits for the CU:**

More frequent repayments provide a liquidity source

Reduces non-repayment risk for the credit union

Opportunity to track the members repayment more closely

Provides opportunity of the credit union to learn more about the member.

**Benefits to the Member:**

More frequent loan payments reduces the payment amount to smaller more manageable payments.

It also provides the opportunity for the member to learn what the credit union is offering as far as new loan products.

**Q & A** Facilitate a 5 minute question and answer session in which you allow participants time to ask questions about loan types and characteristics.

### **PURPOSES FOR LOANS (15 minutes)**

**Lecture** Present a 15 minute lecture in which you introduce the purposes for loans.

There are many reasons why a member may want to borrow money.

Therefore, there are different types of loans to fit the different purposes.

#### **Consumer loans**

These are loans offered to individuals for their personal needs.

They may want to pay for children's school tuition or home improvement.

Other Consumer Loan purposes include wedding costs, small appliance loans such as refrigerators, and stoves.

Consumer Loans are of a higher risk since the loan purpose is not necessarily tied to increase the member's personal wealth or create additional income.

When granting consumer loans, these loans should be for your most trusted and valued member.

#### **Agricultural loans**

These are loans offered to individuals in order to perform an agricultural function.

They may need to buy land, equipment, or supplies.

Agricultural loans are of high risk as well due to the reliance upon good weather to ensure income that is used to repay the loan at the credit union.

#### **Business loans**

These are loans offered to one or more individuals in order to start or improve a business.

Business loans can include the starting of a tailoring business to purchase thread, material and sewing equipment; small grocer where loan proceeds will be used to purchase the first inventory.

They may need to buy land, and equipment.

They may also be wishing to start a business program.

### **METHODS FOR LENDING (25 minutes)• There are several different ways in which a credit union can offer credit to a member.**

#### **Direct lending**

This is the most common way to lend money to a member.

The member comes to the credit union, completes a loan application, and, if the loan is approved, the credit union lends him the money.

#### **Direct Lending with a Vendor**

Member comes to the credit union, completes a loan application with a purpose of buying a refrigerator. Credit union has previously established a working relationship with a local vendor that sells refrigerators. Member signs loan documents and loan proceeds are made payable to the local vendor.

When establishing a working relationship with a local vendor the credit union should have a contract for the vendor to sign.

The contract will be for a specified term and will cover areas of operation between the vendor and the credit union.

**The contract should include:**

Purpose of contract-to provide products/equipment to the credit union members at cost or with a small mark up over cost of the product;

An agreement where the vendor only applies the funds for the purchase of the equipment or product as stated within the loan agreement between the member and the credit union;

An identification or serial number of the equipment (if available) will be provided to the credit union by the vendor;

A paragraph stating the procedures for returning the funds to the credit union if the member decides not to purchase the stated equipment/products within the loan agreement; or in the situation where the equipment or product is no longer available for purchase through the vendor;

How money will be transferred to the vendor from the credit union;

And how the contract may be stopped between the credit union and the vendor prior to contract expiration date.

An attorney hired by the credit union must review all contracts prior to usage.

Why would a vendor want to enter into an agreement with the credit union?

The credit union will recommend members looking for particular products to go to those vendors that are working with the credit union and are selling requested products/equipment;

Credit Union provides a larger customer base for the vendor;

Vendor has the ability to sale products to member that may not have otherwise come to the vendor's store;

Provides long-term customer base for the vendor due to ease of transaction between member-credit union-vendor.

Internationally, the system of Direct Lending with the Vendor has worked to the credit union's advantage.

Members are provided specialized services through this type of agreement.

Credit Union's can closely monitor that proceeds of loan are used as to the purpose as stated within the member loan contract.

Areas to be aware of:

Vendors offering equipment to member, but once loan is signed, vendor switches equipment to one of lesser value than what was originally agreed to with member; Vendor then keeps the difference between what the member was provided through the loan and the lesser cost of the lesser valued equipment;

Vendors that do not keep proper stock available which will make members dissatisfied with the credit union offering this vendor as a provider of products/equipment.

**Case 1 problem:** A husband and wife come into the credit union. They have Kip 60000 in shares in the credit union. They want to borrow KIP 600000 to make improvements on their family farm that they own and operate. They do not owe any money.

**Case 1 suggested answer:** This couple would probably benefit from line of credit. That way, they can withdraw money as they need it for improvements. A guarantor would be required on this loan.

**Case 2 problem:** A member is requesting KIP40000 for feed for his livestock. He is a new farmer just beginning in raising livestock. He has never had a loan before at the credit union.

**Case 2 suggested answer:** Because the member is not experienced in raising livestock and has never had credit before a counteroffer in the amount of KIP 20000 may be given to the member. A guarantor will be required.

**Case 3 problem:** During the month of December a member comes into the CU and requests Kip 100000 for seed to plant sunflowers.

**Case 3 suggested answer:** Credit union should recognize that the month of December is not planting time for sunflowers and that the loan officer should ask the member what the true purpose of the loan actually is. Member then should complete a new application based on true purposes of loan needs.

### **THE DUTIES OF A LOAN PROFESSIONAL (30 minutes)**

Create your own lecture, or use the following.

As a loan professional, you will have many duties to perform.

They are:

- To meet your members' loan needs.
- To maintain good relations with your members.
- To carry out the loan application process.
- To ensure that credit union loans are profitable.
- To comply with credit union policies and procedures.
- To comply with legal requirements.
- Let's look at each of these duties in more detail.
- To meet your members' loan needs

You are the link between your credit union and the money your members wish to borrow.

You should make it your goal to connect your members with the loans that are most beneficial to them. Agricultural loans must be tied to the growth season and harvest; loan repayments must be matched with the member's cash flow.

You do this by knowing your credit union's loan products well and by learning your members' needs. You can learn your member's needs through the loan interview process by asking specific questions: What do you need to borrow money for? ; What is your employment? ; How will the loan funds benefit you? ; After the questions are asked and the answers learned the loan office can then match the loan product to the member's needs.

The loan officer also needs to have a detailed knowledge of the business environment in which the members are involved, have a clear idea of what competitors are offering and a constant desire to look beneath the surface to identify information that is relevant to the credit decision, state of the members affairs and character.

To maintain good relations with your members

The best way to learn your members' needs is to maintain good relations with them. Good relations means to always treat your members with respect and good service.

Listen to what they say they need, and then answer their questions relating to loans. Never be too busy to talk to a member. Make sure your attention is on the member in front of you and not on other work that is sitting on your desk.

You may even need to assist them in filling out their loan applications. Many times this will be the member's first experience in obtaining a loan. The credit union loan officer is there to help the member understand and feel comfortable with the loan process.

It is important that you keep the information they give you confidential. As a loan officer you will learn personal information about your members. This must be kept between you and the member and not discussed with others within the credit union or within the community.

It's also important that you communicate your decision to them in a positive way. Even if the Loan application is rejected, the loan officer should notify the member what they may do to Improve their ability to receive a loan in the future. This may be to reduce the member's expenses, request a smaller loan amount or obtain additional monthly income in order to increase the ability of the member to repay the loan.

You also may need to be available to provide financial counseling to the member. Financial counseling would include how the member may improve their overall economic standing. The loan officer may review the member's personal budget and determine how monthly expenses may be reduced and how to begin to set aside excess monthly income for personal savings

### **Carry out the loan application process**

You must be able to do this efficiently and accurately even while you strive to maintain member relations. This requires the loan officer to do multiple tasks simultaneously: talk to members about the credit union loan products, help members complete loan applications, interview members for loans, complete the loan folder for credit committee review and once loan is approved, prepare loan documents for disbursement. Members come into the credit union at all

times, therefore a loan officer could have many members at different stages of the loan application process.

To ensure that credit union loans are profitable

Of course, the most obvious way to do this is to execute the loan process carefully.

But you can also analyze the loans you have made to see how well they are performing.

You do this by preparing monthly reports relating to the loans you've issued. Reports would include an analysis by loan purpose (agricultural, personal, education) by term (6, 12 months) and collateral (guarantor, physical collateral).

You do this by preparing monthly reports relating to the loans you've issued. Reports would include an analysis by loan purpose (agricultural, personal, education) by term (6, 12 months) and collateral (guarantor, physical collateral).

An analysis of these reports can help you identify problem loan areas. If after analysis you see that those loans made for terms of 12 months have a slower repayment history, the credit union must decide the reason behind this behavior. Is it the loan officer that is not obtaining enough information for credit committee and the board of directors to analyze the loan applications correctly? Or is it the majority of members cannot handle a repayment term of longer than 6 months? Or is it a collateral issue? Are members not repaying when physical collateral is being used? Based on the credit union's analysis, the loan products may have to be adjusted in order to ensure timely loan repayment by the member.

To comply with credit union policies and procedures

This includes procedures set up by the board of directors and the credit committee. Procedures would include: time it should take the loan officer to complete the loan application and folder to present it to credit committee, how the member is to be contacted in cases of loan rejection, loan disbursement procedures and loan repayment procedures. It also includes your credit union's general policies and procedures. The loan officer must be familiar with all credit union policies and procedures to inform and educate members.

To comply with legal requirements

You must take the time to know the laws and regulations that apply to your credit union.

As you cover the steps in the loan application process,

Create your own lecture, or use the following.

As a loan professional, you will need to be completely familiar with the loan application process.

**There are many steps to the loan process. Let's review them now.**

**Step 1: Take the loan application.**

The first thing you need to do is take the loan application

You can either have members complete an application, or you can complete the application as the members provide you with the information. (The Regional Representative may assist the member in completing his/her application.)

**Step 2: Verify application information.**

- Make sure you can read all the handwriting.
- Verify the spelling of the name so that you know it will be correct on all the loan papers.
- Make sure the phone number and address is correct and complete.
- Verify the signature of the loan application with the member share certificate. Are they the same? This verification is to ensure the actual member is the person applying for the loan.
- Through interview with the member determine what the loan purpose is to be, verify sources of income and outstanding expenses.
- Collateral must also be decided: guarantor or physical equipment. If guarantor the guarantor must go through the same approval process as the borrower. If physical equipment, then the credit union must obtain an appraisal of the value of the collateral to be held.
- If additional paperwork is needed, request from member at this time. Additional paperwork may include: title work to collateral, proof of income/cash flow, proof of expenses (copies of utility bills).

**Step 3: Calculate loan payments.**

You need to determine what the loan payments will be and how often: monthly, or quarterly or matched to the member's cash flow.

Make sure you disclose and can explain your calculations to the applicants.

**Step 4: Make the loan decision recommendation.**

Questions to ask yourself when determining the loan recommendation:

- Is the application complete, dated and signed?
- Is the amount reasonable for the purpose and maturity?
- Does the maturity correspond to the loan purpose?
- Has all the information given by the applicant been verified?

- Is the applicant stable, with regards to residency and employment?
- What income is to be used to repay the loan?
- Can one reasonably expect income to continue until the loan is paid off (is there an adequate repayment source)?
- Can the member properly manage all debt including the new loan payment with the credit union?

Does the member have any remaining income after the member pays all expenses?

(This is important in situations of emergency where member needs additional income )

Does the member have dependents (persons that are reliant upon the member's income)? If so, be sure to include additional costs for clothing and food.

- If this is a business or production loan a field visit should be scheduled to the member's place of business to ensure the following:
  - Is the property of the business well maintained?
  - Does the business have adequate staffing/workers to carry out the work as required?  
Example: Farmer has multiple acres of land, is there enough field workers for planting and harvest?
  - Is there enough equipment to cultivate fields?

If the member has a small business, are the shelves well stocked with inventory? Are customers of the small business making payments on time for purchases from the small business?

(Example: member owns small grocery store. Are there many customers that buy groceries on credit? If so, how is the store paying for additional inventory?)

- Based on the information you have received, you need to decide whether to state the loan should be approved or rejected.
- Be sure to follow credit union policy.
- Refer the loan application and corresponding documentation to the credit committee.
- Credit committee makes recommendation to the board of directors.
- Board of directors makes approval or rejection of loan.
- Board of directors cannot make approval of loan without the agreement of approval from credit committee.

### **Step 5: Communicate your decision to members.**

- Take the time to make certain the applicant understands your decision.
- If the decision is positive, make sure they know their responsibilities for repayment.
- If the decision is to decline the loan, recommend alternatives. (lower requested loan amount, reduction of outstanding expenses)

### **Step 6: Prepare the necessary loan documents.**

- Be sure to get the member's signatures on all the loan documents.
- If there is a guarantor, be sure guarantor signs required documents at same time as member signs the loan contract.
- If physical collateral is being held for the loan be sure all paperwork is in loan folder.

### **Step 7: Monitor loans.**

- Set up a system that alerts you when a member misses a payment.
- Create a procedure for collecting on delinquent loans and coordinate with the credit union manager and credit committee.
- Close the lecture by reminding participants that this was just an overview of the loan process. It will be covered in more detail in a later chapter.

**As a loan professional, expectations**



#### Attendance

Come to work every day.

Come to work on time.

Allow enough time to get to work so that unexpected delays won't make you late.

Take sick days only when you are sick.

Schedule medical appointments and other appointments on your own time

#### .Confidentiality

Your members will be telling you private information about themselves.

This is information that should be kept confidential.

Credit union business should never be discussed outside of work.

Your members are trusting you—make sure to keep it that way.

It is inappropriate to discuss a member's earnings with others, including coworkers.

- **Loyalty**

- It is important for you to stand by your credit union's policies and procedures, even if you disagree with them.
- When you are in public, avoid criticizing the credit union. Instead, be willing to discuss how the credit union benefits its members.

- **Dedication**

- Be dedicated to your job.
- Instead of waiting to be told to do something, look for things that have to be done.
- Volunteer to do extra work.
- Take part in credit union functions within the community.
- Look for opportunities to grow and improve.

- **Honesty**

- Keep accurate records on all the transactions you conduct with members.
- It is unacceptable to accept cash, supplies, or other bribes from members.
- If you make a mistake, admit it. If you try to hide the mistake, it will only get worse.

Tell the truth—both to your members and your coworkers. You will gain the respect of others and they will seek you out for help.

- **Knowledge**

- Be familiar with all the products and services the credit union offers.
- Know your credit union's policies and procedures.
- Stay informed with respect to local lending regulations.

- Conclude by telling students that, if they work hard to fulfill these expectations daily, they will be effective loan professionals.

- **SKILLS REQUIRED OF A LOAN PROFESSIONAL (20 minutes)**

Create your own lecture, or use the following.

It is one thing to fulfill the expectations your credit union has of you.

However, to completely carry out the duties of a loan professional, you will also need to have a number of skills.

- Let's review these skills now.

- **Interpersonal skills**

- To get to know your members, you will need to listen to their concerns and assess their needs.
- This means you must be able to listen actively.
- You must also be able to show empathy to their situation.
- At times you will need to be patient with them. They may not understand the loan process as well as you do, and you may have to explain it more than once.
- You must also be able to convey information to members.
  - What they must do to get a loan.
  - What their responsibilities are for repaying a loan.
  - Why a member didn't get a loan.
- This means you must be clear and articulate, and you must ensure that members understand what you are telling them.

- **Organizational skills**
  - All documents pertaining to a member's application must be kept on file.
  - Loan applications must be kept.
  - Loans must be documented.
  - Specific forms must be filled out.
  - It is important that you be organized so that you know how to find these documents when you need them.
  - Also, you must be able to handle loans that are in different stages of completion.
  - Some will be at the application stage.
  - Some will be approved, but not yet dispersed.
  - Others will be in various stages of repayment.
  - It is essential that you be able to keep track of loans in all these stages so that you can follow up when necessary.
- **Analytical and judgment skills**
  - You must be able to take information that members give you, and then determine if they qualify for a loan.
  - This requires both that you have good analytical skills and that you use good judgment.
  - You need to be able to recognize when you must obtain more facts.
  - You need to be willing to follow up if members can't provide specific information at the time of application.
  - You must remain objective.
  - Avoid making decisions based on a person's appearance.
  - Instead, make them based on the facts at hand, and on the credit union's guidelines.
- **Flexibility**
  - Things change and loan professionals must be able to adjust to changes.
  - Job priorities change.
  - Members change their minds.
  - Unexpected events will occur.
  - You must remain calm even when events are not
  - You must remain calm even if the member is upset.
  - You must be able to handle extremely busy situations.
- **Professional appearance**
  - Your appearance should inspire trust in the member. After all, he will be telling you highly personal information.
  - Dress professionally.
  - Make sure you are clean and groomed.
  - Avoid snacks or gum chewing.
  - Keep your work area free of clutter.
- **Knowledge of credit union policies and procedures**
  - Credit union policies and procedures exist to protect members from loan losses, and to ensure consistency in lending.
  - You must adhere to the policies even if you think they are wrong. If a portion of the policy or procedure is not working for your credit union, the loan officer may make a recommendation for the credit committee to discuss with the board of directors. Until a final decision is made to change the loan policy and corresponding procedures, the written policy and procedures format must be followed.

Loan officers must always be objective; if a loan application comes to the credit union and it is a close friend or relative of the loan officer, the loan officer should tell the credit committee upon submission of application for review.

It is unacceptable to make exceptions for friends or family members.

- Some of these skills that we have just discussed you already have.
- Others you may need to develop as you gain lending experience.
- As long as you are willing to continue learning, you will continue to grow and improve as a loan professional.
- Regardless of whether credit is closed-end or Line of Credit it can also be either secured or unsecured.

### **Secured loans**

Use collateral. (Note: at this time Credit Unions do not use collateral on loans due to the difficulty in securing a lien and the difficulties of repossessing and selling collateral if borrower defaults on loan.)

This is a tangible asset that belongs to the member.

The member agrees to hand this asset to the credit union in the event of a loan default.

### **Unsecured loans**

- Have no collateral.
- The member's promise to pay is guaranteed only by his signature.
- Are often called "signature loans".
- Are risky loans because, if a member defaults, the credit union may not be able to claim any of the member's assets.
- Guarantee loans-is a type of unsecured loan.
- Loan is guaranteed by another individual stating that if member defaults guarantor will take over repayment responsibilities of the loan.

There are three factors that will influence how the money will be repaid.

- The first is interest rate.
- The second is *maturity*.
- The third factor is *terms of repayment*.

- Let's look at each of these factors in more detail.
- Interest rate
  - The interest is the amount a member pays for the loan.
  - The interest rate is a percentage of the loan amount.
  - There are two types of interest rates a credit union might offer: *fixed rates* and *variable rates*.

### **Fixed rate Flat**

- With a *fixed rate*, the interest rate stays the same throughout the duration of the loan.
- Closed-end loans often have a fixed rate.

### **Variable rate Declining**

- Variable rates adjust up and down throughout the loan term based on an index or a formula.
- Variable rates allow a credit union to limit its interest rate risk because they enable the credit union to avoid committing to low interest rates if there is a possibility the rates will rise.
- Variable rates are set using an *index* or a *formula*. This index can be an outside index or one that the credit union sets based upon its own *cost of funds*.
- A credit union's *cost of funds* is an amount based on what the credit union is paying for the cost of using the funds. Costs of funds may include the interest charged on

external credit or the use of funds of member shares represented by the cost of dividends or interest on member savings accounts.

- Once the credit union chooses an index, it can then add a percentage that covers the cost of the loan plus some return. This percentage is referred to as a *spread*.
- The selected index plus the spread equals the variable rate.
- Open-end loans (such as credit cards) often have variable rates, but closed-end loans can also have variable rates.

### The formula

The calculation used to arrive at the periodic payment amount assumes that the first payment is not due on the first day of the loan, but rather one full payment period into the [loan](#).

While normally used to solve for  $A$ , (the payment, given the terms) it can be used to solve for any single variable in the equation provided that all other variables are known. One can rearrange the formula to solve for any one term, except for  $i$ , for which one can use a [root-finding algorithm](#).

The [annuity formula](#) is:

$$A = P \frac{i(1+i)^n}{(1+i)^n - 1} = \frac{P \times i}{1 - (1+i)^{-n}} = P \left( i + \frac{i}{(1+i)^n - 1} \right)$$

Where:

- $A$  = periodic payment amount
  - $P$  = amount of [principal](#), [net](#) of initial payments, meaning "subtract any down-payments"
  - $i$  = periodic [interest](#) rate
  - $n$  = total number of payments
- For a 3-year loan with monthly payments,  
 $N = 3 \text{ years} \times 12 \text{ month/year} = 36 \text{ month}$

Note that the interest rate is commonly referred to as an annual percent (e.g. 8% APR), but in the above formula, since the payments are monthly, the rate  $i$  must be in terms of a monthly percent. Converting an annual interest rate (that is to say, annual percentage yield or APY) to the monthly rate is not as simple as dividing by 12, see the formula and discussion in [APR](#). However if the rate is stated in terms of "APR" and not "annual interest rate", then dividing by 12 is an appropriate means of determining the monthly interest rate.

### EXPECTATIONS OF A LOAN PROFESSIONAL (15 minutes)

As a loan professional, your credit union has certain expectations of you. Let's review them.

Attendance

Come to work every day.

Come to work on time.

Allow enough time to get to work so that unexpected delays won't make you late.

Take sick days only when you are sick.

Schedule medical appointments and other appointments on your own time.

Confidentiality

Your members will be telling you private information about themselves.

This is information that should be kept confidential.

Credit union business should never be discussed outside of work.

Your members are trusting you—make sure to keep it that way.

It is inappropriate to discuss a member's earnings with others, including coworkers.

**Loyalty**

It is important for you to stand by your credit union's policies and procedures, even if you disagree with them.

When you are in public, avoid criticizing the credit union. Instead, be willing to discuss how the credit union benefits its members.

**Dedication**

Be dedicated to your job.

Instead of waiting to be told to do something, look for things that have to be done.

Volunteer to do extra work.

Take part in credit union functions within the community.

Look for opportunities to grow and improve.

**Honesty**

Keep accurate records on all the transactions you conduct with members.

It is unacceptable to accept cash, supplies, or other bribes from members.

If you make a mistake, admit it. If you try to hide the mistake, it will only get worse.

Tell the truth—both to your members and your coworkers. You will gain the respect of others and they will seek you out for help.

**Knowledge**

Be familiar with all the products and services the credit union offers.

Know your credit union's policies and procedures.

Stay informed with respect to local lending regulations.

Conclude by telling students that, if they work hard to fulfill these expectations daily, they will be effective loan professionals.

**SKILLS REQUIRED OF A LOAN PROFESSIONAL (20 minutes)****Interpersonal skills**

To get to know your members, you will need to listen to their concerns and assess their needs.

This means you must be able to listen actively

You must also be able to show empathy to their situation.

- At times you will need to be patient with them. They may not understand the loan process as well as you do, and you may have to explain it more than once.
- You must also be able to convey information to members.
  - What they must do to get a loan.
  - What their responsibilities are for repaying a loan.
  - Why a member didn't get a loan.
- This means you must be clear and articulate, and you must ensure that members understand what you are telling them.
- **Organizational skills**
- All documents pertaining to a member's application must be kept on file.
- Loan applications must be kept.
- Loans must be documented.
- Specific forms must be filled out.
- It is important that you be organized so that you know how to find these documents when you need them.
- Also, you must be able to handle loans that are in different stages of completion.
- Some will be at the application stage.
- Some will be approved, but not yet dispersed.
- Others will be in various stages of repayment.
- It is essential that you be able to keep track of loans in all these stages so that you can follow up when necessary.

## **Analytical and judgment skills**

- You must be able to take information that members give you, and then determine if they qualify for a loan.
- This requires both that you have good analytical skills and that you use good judgment.
- You need to be able to recognize when you must obtain more facts.
- You need to be willing to follow up if members can't provide specific information at the time of application.
- You must remain objective.
- Avoid making decisions based on a person's appearance.
- Instead, make them based on the facts at hand, and on the credit union's guidelines.

## **Flexibility**

- Things change and loan professionals must be able to adjust to changes.
- Job priorities change.
- Members change their minds.
- Unexpected events will occur.
- You must remain calm even when events are not.
  - You must remain calm even if the member is upset.
  - You must be able to handle extremely busy situations.

## **Professional appearance**

- Your appearance should inspire trust in the member. After all, he will be telling you highly personal information.
- Dress professionally.
- Make sure you are clean and groomed.
- Avoid snacks or gum chewing.
- Keep your work area free of clutter.

## **Knowledge of credit union policies and procedures**

- Credit union policies and procedures exist to protect members from loan losses, and to ensure consistency in lending.
- You must adhere to the policies even if you think they are wrong. If a portion of the policy or procedure is not working for your credit union, the loan officer may make a recommendation for the credit committee to discuss with the board of directors. Until a final decision is made to change the loan policy and corresponding procedures, the written policy and procedures format must be followed.
- Loan officers must always be objective; if a loan application comes to the credit union and it is a close friend or relative of the loan officer, the loan officer should tell the credit committee upon submission of application for review.
  - It is unacceptable to make exceptions for friends or family members.
- Some of these skills that we have just discussed you already have.
- Others you may need to develop as you gain lending experience.
- As long as you are willing to continue learning, you will continue to grow and improve as a loan professional.

## **IMPORTANCE OF THE LOAN APPLICATION FORM (10 minutes)**

- Present a 10 minute lecture in which you emphasize the importance of having a loan application form.

- Loan application forms are found within the CU-Mbr Loan forms folder.
- These are the key points you should make.

The loan application is an important document in the loan request process. It contains much of the information that the credit union needs to make a decision about granting a loan.

It is important that this document be properly understood and effectively used.

Loan application may be filled out by member, CU representative, or with the assistance of the Regional Representative.

The information should provide the majority of information needed to make the lending decision.

The application should be verified through the loan interview, verification of a member's assets and debts, and possibly a site visit.

When evaluating the loan application, you should consider the following:

Amount of loan

Purpose of the loan

Collateral offered, if any, the value and the condition of it (credit union employee should do a physical inspection)

Total monthly obligations of applicant

Number of dependents

Length of residence of applicant

Employment of the applicant and the employment length

Monthly income of the applicant (stable and sufficient)

Credit and savings history at credit union

Personal and credit references

To be fair to all loan applicants, it is important to ask the same questions of every person. A loan application can help you do this.

### **REVIEW OF THE LOAN APPLICATION FORMS (40 MINUTES)**

There are two loan application forms:

Loan Application Form And Business Plan For Short Term Credits (loan terms of <12 months);

Loan Application Form And Business Plan For Investment Loans (loan terms > 12 months)

Review of Loan Application Form And Business Plan For Short Term Credits:

**First box** in the application is the section for the member to state amount and purpose requested for the loan application, the member's identification information: Credit application number at the CU, Member Account Number, Date of Application, Name of Member, Family Name, Last Name, as well as Region, Rayon and Village information.

**Second box** includes information on land that is owned by the member. Member needs to provide information on owned property for the following areas: address, category, document of ownership, document number, when the document was issued, number of hectares owned, value of hectares and who is registered landowner.



**Third box** includes information about crops grown and their corresponding income and expenses associated with the crops. Information includes: Crop type, Number of Hectares of the crop, per crop type the number of hectares used, Total product production, anticipated price per product, anticipated total amount of product, cost per hectare, total cost of product(s).

**Fourth box** requests information on Input and Equipment and if there are any corresponding liabilities of the member for the listed equipment. Information must be obtained on Title of equipment, number of listed equipment, and their total cost. If a debt is owned on equipment the creditor must be stated along with the indebted amount.

**Box five** is the Number and Price of Livestock. Information requested is the type of livestock, number of, price per animal, and total price of livestock. If the animal produces a product the type of product must be listed (Ex: milk, cheese, wool), number of animals producing, total production and its unit price, and the total amount earned, per animal cost to the farmer and total cost.

The last box on the first page is the information box for who the member's guarantor will be. Full name, passport number and signature of guarantor is required.

There is a section for the Executive Representative of the Village of the member to sign and date stating the member completing the loan application is a resident of the stated village/rayon.

On the second page there is a Profit and Loss Statement box: Income of the Product of the farmer, Production, unit price and total amount.

Expenditures box includes: Product, production, unit price and total amount in expenditures. Land rent expense, other expenses and the area of where expenses are totaled.

The loan officer then takes the Gross profit (total income-total expenses) to calculate the Net Profit of the member.

The next section is the Cash flow. Within the Cash flow Section the loan officer calculates the inflows of cash (income) minus the outflows (expenses) of the borrower to determine the cash flow situation of the borrower. The end result is to determine if the member has a positive or negative cash flow situation.

If the member has a positive cash flow situation then the credit union determines whether or not the borrower can repay an additional debt (the credit union loan) responsibly.

If the member has a negative cash flow situation then the credit union would recommend to the borrower that he/she cannot obtain a loan through the credit union because there is not enough cash flow (income) to cover the additional debt of the credit union loan payment.

The member signs and dates the loan application as well as the representative from the Regional Advisory Center.

Review of Loan Application Form And Business Plan For Investment Long Term Credits:

**Part A: Boxes 1-5** are the same as under the Short Term Loan application. The Executive Representative of the Village has an area of which he/she signs and dates certifying the member is a resident of the village/region.

**Part B:** Information on Banks-member must state if he/she has any accounts at other banks.

**Part C:** Planned Expenditures for Investment and Working Capital-includes 3 separate boxes for the member to provide information of how the credit union loan will be used

**Section 1. Investment Expenditures:**

Inputs and equipments: Name/type of equipment, number of and total price;

Number and price of livestock-type of livestock, number of, per livestock value, total livestock value;

Other investments-Type of investment, Number of, Unit price and Total Price.

**Section 2. Working Capital Expenditures:** includes the type of expenditure the member would like to purchase and the total amount.

Both the Investment and Working Capital Expenditures are totaled to provide the credit union loan officer the full amount of which the member is requesting within the loan application.

**Section D:** Credit Needed-is the section in which the member states the total amount of expenditures planned corresponding with the use of the borrowed funds from the credit union; type and amount of private investment-what if any the member will contribute towards the planned expenditure; Investment amount from other sources (if any)-if the member is borrowing any funds from other sources; Loan amount required from the Credit Union-must be indicated the final amount the member is requesting in loan funds.

**Section E:** Loan Repayment Table-the credit union loan officer calculates the loan principal and interest that the member must repay along with the stated loan repayment dates for the loan purpose.

**Section F:** Loss and Profit Statement-calculates the members income and expenditures to determine the Net Profit of the member borrower.

Cash Flow-determines the inflows (income) and the Outflows (expense) of the member borrower to determine if there is a positive or negative cash flow for the member based on his/her employment/business activity.

**Section G:** Offered Collateral-if there is to be collateral offered a collateral determination and declaration form must be completed and attached to the loan application;

Or if there are guarantors, the same loan application process must be completed for each guarantor.

Signatures-member must sign as well as the private advisor that may have helped to complete the application.

What happens if upon review by the loan officer, the loan applicant's information does not comply with the loan policy? What should the loan officer do?

Loan officer should discuss with the member those areas of which fall outside of the loan policy.

Examples would be if the member is requesting more money than the loan purpose allows, the new loan payment is more than the member can afford to pay, physical collateral offered is not of the same value as the requested loan amount.

The loan officer could recommend the member the following:

More money than the loan purpose allows-if the member is requesting they need 5000000 for the planting of corn, and the credit union realizes the member only needs 3000000 for this purpose, the loan officer should counsel the member that the loan amount requested does not match the loan purpose. The loan officer could recommend to the member the lesser amount of 3000000 to enter within the loan application.

The new loan payment is more than the member can afford to pay-after the loan officer analyzes the loan and realizes the member does not have sufficient income to pay the new loan payment, the loan officer should recommend the member to borrow a lesser amount in order to lower the monthly loan payment.

Physical collateral offered is not of the same value as the requested loan amount-the appraisal of the physical collateral that the member is offering for security comes back less than the amount applied for by the member. The loan officer needs to explain to the member that the collateral is only worth a certain amount and therefore the loan amount must be tied to the collateral's value.

Loan officers need to work with members to try and find solutions for members to obtain loans through the credit union if the loan officer believes the member is responsible and will make all credit union loan payments.

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## **LOAN INTERVIEWING**

Purposes for the loan interview

Preparing for the loan interview

Closed-end questions

Leading questions

Behavioral questions

Steps for conducting the loan interview

Follow-up questions

Following up after the loan interview

Write comments and critical points you want to make in the margins of this Instructor's Guide. Make copies of the case study at the end of this chapter and distribute them to participants,

OR

Be prepared to read each case to participants before they analyze them.

## **PURPOSES FOR THE LOAN INTERVIEW (10 minutes)**

A successful lending program follows the loan application with a loan interview.

The interview should be conducted by the loan officer, manager or credit committee depending on the size of the credit union and the size of the loan.

The interview will be conducted with the applicant and may also include any guarantors on the loan.

The larger and more riskier the loan, the more extensive the interview will be. It is helpful if the credit union interviewer:

- Elaborate on the information in the application-know the borrower
- Provide credit counseling about the wise use of credit-borrowing
- Credit union is for use of the community, defaulters on loans will ruin the ability for future work of the credit union.
- Determine the reliability of the applicant according to their
  - personal history and references
- Establish a personal relationship- make them understand that this is their credit union.
- Sell other credit union services and educate the member about the credit union philosophy-use this personal time wisely-

## **IMPRESS THE BORROWER.**

### **Interview Guidelines**

- The interview is best performed when the interviewer has a genuine interest in the problems of the member. Members in need of financial assistance are sensitive to the manner in which they are received.
- There are several guidelines which should be followed to develop an interview:
  - **Greet the members:** Your first goal is to put the applicant at ease. Call the member by name, make casual conversation, and be interested sincere, and natural.
  - **Getting acquainted:** Talk for a few minutes before referring to the application. Remember that loan interviews are uncomfortable for many members. Any effort you make to get acquainted reduces member's anxiety.
  - **Maintaining confidentiality:** Prior to the interview, you should have checked your area for privacy. Information should never be repeated to other members nor should information about other members be told to the interviewee. In fact, you should not even repeat member's information to coworkers who do not need to know.
  - **Listening:** This is the most important part of effective interviewing. You must determine the needs of your member and can only do this by listening. Active listening means involving yourself in the members' message. Show by the use of certain phrases such as "oh," "I see" or "I understand" that you are indeed listening and understanding.
  - **Take your time:** Rushing members will not get the information you need. Give them time to respond to your questions and to finish their thoughts.
  - **Ask Open Ended Questions:** Ask Questions that require more than a "yes" or

“no” answer. This will open the door to more thought out responses. Questions beginning with words such as: what, who, when, where, why and how should help to encourage the applicant to speak.

- **Keep Control:** The interviewer rather than the member, should conduct and control the course of the interview. Preplan the interview so that you have an agenda of questions or items that you want to cover. You may want to use an interview guide when going over the loan application for assistance in completing the interview.
- **Content of the Interview:** It is most important that the credit union gain a complete understanding of the member’s activity and the state of development.

The final, and most important, reason to conduct a loan interview is to evaluate the three C’s of lending.

- A person’s character.
- A person’s capacity to repay the loan.
- The collateral a person has to back up the loan.
- Point out that they will learn more about the three Cs of lending in the next chapter.
- Close the lecture by telling students that interviews can be conducted in person or over the phone.

## **PREPARING FOR THE LOAN INTERVIEW**

- You will be most effective during the loan interview if you take some time to prepare for it.
- There are four key steps you can take to prepare for the loan interview.
  - **Step 1:** Review the loan application.
  - **Step 2:** Plan the approach you will use for the interview.
  - **Step 3:** Write some interview questions.
  - **Step 4:** Prepare the interview setting.
- **Let’s examine each of these steps in more detail.**
- **Step 1: Review the loan application.**
- You can learn a lot about a person by reviewing his loan application.
- Here are some of the items to look for in reviewing the application.

### **Is the application complete?**

Has the applicant provided all the requested information?

If not, plan to ask for that information during the interview.

### **Is the application consistent?**

Is the address on the application the same one you have on record at the credit union?

Does one place on the application indicate one type of marital status, while another place indicates a different marital status?

Is the name in the printed box spelled the same as the name in the signature box?  
Inconsistencies on the application may simply mean that the applicant made a mistake.  
However, they could also mean the applicant is being untruthful.  
Plan to ask about these inconsistencies during the interview.  
Does the application raise any concerns?  
In looking at the application, do you see any clues that indicate the applicant may not be willing or able to repay the loan?  
Does the applicant have a spotty employment history? Are there gaps in the dates of employment? If so, plan to ask about them in the interview.  
Has the applicant listed a reference that lives far away? This reference could be a longstanding friend. But it could also be a sign that the applicant had trouble finding references. Plan to ask about this in the interview.  
Is there some missing information on the application? Simply plan to ask for this information in the interview. However, be watchful of the applicant's response. If he seems reluctant to give the information, he may be hiding something. On the other hand, if he simply needs time to look up the information, give it to him.  
What is the general feeling you get in looking at this loan application? You want the application to give you a profile of someone who can and will repay the debt.  
Is the collateral offered for the loan adequate to cover the loan amount?

## **Step 2: Plan the approach you will use for the interview.**

Remember that the purpose of the interview is to achieve four things:  
Establish a relationship with the member.  
Get information.  
Give information.  
Determine if the applicant meets the three Cs of lending: Character-is the member of good, sound character? In other words, is the member responsible enough to make timely payments to the credit union?  
Capacity-does the member's loan application reflect the capacity (income) to be able to pay all outstanding debt, plus the additional debt of the new loan payment?  
Collateral-if there is physical collateral being offered as security for the loan is the value of the collateral adequate?

The best way to plan your approach to the interview is to structure it around these four objectives.  
How will you establish a relationship with your member? Plan to listen to the member's needs and give him the precise loan he needs.  
How will you get information about the applicant's creditworthiness? The best way to do this is to ask for the information you need. When you ask about inconsistencies on the application, be sure to be tactful.  
How will you provide information to the applicant? The best way to do this is to make a check list containing the things you want to share. This should include information about the credit union and about the member's loan.  
How do you determine if the applicant meets the three Cs? You can determine character by assessing the applicant's truthfulness and forthrightness in the interview. You can determine capacity by reviewing the financial information. You can determine collateral by reviewing the applicant's assets.

## **Step 3: Write some interview questions.**

It pays to have a prepared list of questions when you go into the interview.

Be sure that the questions you write will get the responses that you need.

There are three types of questions you can use in an interview.

**Closed-end questions.** Closed-end questions do not encourage a member to open up. Ask these questions when you need simple, factual responses, such as name and income.

**Leading questions.** Leading questions prompt the member to answer in a certain way. These should be used only when you are attempting to guide the member to a certain decision. For example, if the member wants more money than he is capable of repaying, you might say, "How would you like a loan that you can repay in a year?" Avoid asking leading questions to determine a person's ability to pay. If you say, "Will you be able to repay the loan?" a member is going to say "yes" whether or not it is true.

**Behavioral questions.** These are questions that can't be answered with a "yes" or "no". Instead, they require the member to talk about how he has handled credit in the past. For example, let's say you have a new member and you are trying to learn how sincere he is about repaying the loan. You might ask the following behavioral question. "Think of a time in your past where you owed money, and could not immediately repay it. Describe the situation. What did you do?" The member's answer will reveal how he goes about resolving financial problems.

#### **Step 4: Prepare the interview setting.**

You want to make the interview environment as comfortable as you can for the applicant.

This will put the applicant at ease and make him feel comfortable in answering questions.

Use a quiet, private place, preferably a room with a door that can be closed.

Make sure the space is clean and uncluttered.

Make it clear to others that you don't want to be interrupted.

Allow enough time for the interview.

Look at the interview location from your member's point of view. Would you be comfortable answering personal questions in this environment?

If you consistently use these four steps to prepare for your loan interviews, you will find that you get valuable information about your members during the loan interview.

#### **. CASE STUDY—PREPARING FOR THE LOAN INTERVIEW (30 minutes)**

Facilitate a 30 minute case study. Tell participants that you will read a series of questions.

After the question, they should write down whether the question is:

Closed-end .Leading Behavioral.

- To manage your time, allow about 5 minutes to read the questions, and 5 minutes to discuss the answers.

**Here are the questions you should read.**

**Question #1:** Do you think you need a school fees loan?

**Question #2:** How did you handle your finances when you lost your job?

**Questions #3:** What do you sell at the market?

**Question #4:** Tell me how you plan to budget for this loan.

**Question #5:** Will you be able to pay this loan within twelve months?

**Question #6:** On your application, the references section is blank. Can you provide me with some references?

**Here are the answers to the case study questions.**

**Question #1:** Do you think you need a school fees loan?

**Answer:** This is a leading question because the interviewer is suggesting a type of loan.

**Question #2:** How did you handle your finances when you lost your job?

**Answer:** This is a behavioral question because the interviewer is asking the applicant to describe how he behaved under a set of circumstances.

**Questions #3:** What do you sell at the market?

- **Answer:** This is a closed-end question because the applicant need only give a short, factual answer.

- **Question #4:** Tell me how you plan to budget for this loan.

- **Answer:** This is a behavioral question because the interviewer is asking the applicant to describe his plans for managing the loan.

- **Question #5:** Will you be able to pay this loan within twelve months?

- **Answer:** This is a leading question because the interviewer is implying that the loan needs to be paid within a year.

- **Question #6:** On your application, the references section is blank. Can you provide me with some references?

- **Answer:** This is a closed-end question because the applicant need only give the names and addresses of some references.

- Once you have reviewed all the case study questions and answers, use any remaining time for student questions.

**CONDUCTING THE LOAN INTERVIEW (15 minutes)**

- There are six steps you can take to make a loan interview successful.

- **Step 1: Start the interview on time.**

- An applicant is very likely to be nervous when coming in for a loan.
- If you make the applicant wait for a long period of time, you make the nervousness worse.
- A good rule is to greet the applicant within five minutes of the scheduled starting time.

- **Step 2: Put the applicant at ease.**

- One of the best ways to handle an applicant's nervousness is to put him at ease.
- To do this, introduce yourself as soon as you greet the applicant.
- If you know the applicant's name, use it. Otherwise, ask for the pronunciation, then repeat the name to help you remember it.
- Plan to use the applicant's name throughout the interview. It sends the message that you think the applicant is important.
- Show respect to the applicant at all times. Offer coffee or tea.
  - Use small talk to break the ice by asking him. You might talk about the weather, a



common acquaintance, a person you know who has a similar name. Simply find something the two of you have in common and get the member to talk about it.

- Once the applicant starts talking, the tension will be reduced and the interview will go more smoothly.

○ **Step 3: Tell the applicant what to expect from the interview.**

- The applicant will be uncertain and nervous about the interview process.
- Put him at ease by describing the process right away.
- Then describe what you will be looking for in the interview.
- First, you will learn why the member wants the loan. You do this to make sure he will get the exact loan he needs.
- Next, you will ask questions relating to the loan application.
- Then you will provide information about the loan.
- Encourage him to ask questions at any point during the interview.
- Tell the applicant how long you expect the interview to last.

○ **Step 4: Get the applicant to talk.**

This is probably the most important thing you can do in the interview.

- If you can make an applicant comfortable, you will be able to ask all kinds of questions—including some of the tough, personal questions relating to his financial situation.
- To some degree, your ability to get a person to talk will depend on his credit standing.
- A person with a good credit history will probably answer your questions willingly.
- However, a person with a poor credit history may not be as forthcoming with the required information.
- You need to gain this person's trust.
- Start with an easy question. For example, you might say, *"Tell me about the credit you've had in the past."* Or you could say, *"With respect to your finances, what are you proud of? Is there anything you'd do differently?"*
- Once the applicant starts talking, you can weave in the more difficult questions.
- Be sure to ask follow-up questions. You do this by listening carefully to what the applicant tells you, then asking questions relating to his answer.
- For example, let's say that you've asked the applicant why he wants the loan and he tells you he needs the money to buy a car so he can drive to his new job.
- Some interviewers would accept that as an answer, but you can get more information by asking follow-up questions about the job. For example, you might say *"Tell me about your new job? What will you be doing? How much will you be earning?"*
- From the member's answers to these questions, you can determine if the job seems stable, and you can check for consistency by comparing a member's verbal answers against those on the application form.
- Sometimes when you get an applicant to talk, he may get upset.
- Pay close attention when this happens. The member may be trying to hide something, but he also may simply be nervous.
- To handle this, remain calm, but continue to probe for the information you need.
- Tell the member that you understand he is in a difficult situation, but you need this information in order to help.
- Ask your questions in a non-threatening way, and work hard to help the member maintain his confidence.

- **Step 5: Listen attentively.**
  - Once you have gotten the applicant to open up, it is important for you to listen attentively.
  - While you listen, show empathy. Make sure the applicant knows you understand his situation.
  - Listen objectively. Avoid jumping to rash conclusions. If the applicant says something that concerns you, ask follow up questions to gain further understanding.
  - As the applicant talks, pay attention to detail. He may disclose further information in the interview that can help you in making your decision.
- **Step 6: Tell applicant what comes next.**
  - One of the most difficult times for the applicant will be waiting to hear your response. To make this time easier, tell the applicants the steps that their loan application will go through. Include your estimate of the timing.
  - Also, be sure to let the applicant know if you need any additional items or information from them.
  - Finally, make no guarantees to the applicant. If you make a guarantee and then later find something to cause you to deny the loan, you will create great distress for the applicant.

### **CASE STUDY—ASKING FOLLOW-UP QUESTIONS (20 minutes)**

Facilitate a 20 minute case study. Allow 10 minutes for participants to answer the case study questions and 10 minutes to discuss the answers.

To facilitate the case study, you can either copy the case study page at the back of this chapter and distribute it to students, or read each case to students, allowing time after each reading for students to respond.

If you read the cases to students, allow roughly 2 ½ minutes per case.

When you discuss the answers with students, first allow them time to share their answers, and then provide the suggested answers.

When you provide the suggested answers, tell students that there is no single correct answer. Loan interviewing is a flexible process that allows for many options.

- **Case 1 applicant statement:** “I need this loan because last month I sent all my money to my ailing cousin.”
- **Case 1 suggested follow-up:** What illness does your cousin have? Does your cousin plan to repay you? Will you be sending more money to your cousin?
- **Case 2 applicant statement:** “My son wants to go to school next year.” (Note: On the application, the son’s earnings were listed as income.)
- **Case 2 suggested follow-up:** Will your son continue to work after he starts school? How do you plan to adjust for the earnings after he leaves his job and goes to school?
- **Case 3 applicant statement:** “I am two months late on my rent because I needed the money to fix the car.”
- **Case 3 suggested follow-up:** That’s a difficult situation. Tell me how you arrived at the decision to delay the rent?
- **Case 4 applicant statement:** “I plan to open a vegetable stand in the market.”
- **Case 4 suggested follow-up:** Will you be doing that as an additional job? Will you be leaving your current job to do this?
- After you have discussed all four cases, answer any questions students have.

## **FOLLOWING UP AFTER THE LOAN INTERVIEW (5 minutes)**

- Even when the loan interview is over, you still have two important duties to perform.
  - First, you need to keep track of and follow up on any information or material the applicant still owes you. For example, if the member says he will get back to you with the phone number of a reference, you need to follow-up if he doesn't call you when he says he will.
  - You may feel that this is the applicant's responsibility—not yours. However, consider the possibility that the member was very nervous during the interview and may not have understood his duty to get this information to you.
  - Your second duty applies to ensuring that the credit committee and board of directors will review and act on the application when you told the member they would. If the committee and board can't review the application for some reason, you need to inform the member so he isn't worrying about the loan status.
- If you do these two duties, and if you keep the member informed of the loan status, it will make his wait much easier.
- We have now covered the loan interviewing process. In the next chapter, you will learn how to analyze the information you have collected.

## **LOAN INTERVIEWING CASE STUDY**

During the loan interview, you will have many opportunities to learn about the member. The key is to listen to what the applicant is saying, then to ask follow-up questions. Following are four statements. Assume that an applicant has made these statements to you in an interview. Write a follow-up question for each statement.

1. I need this loan because last month I sent all my money to my ailing cousin.
2. My son wants to go to school next year. (Note: On the application, the son's earnings were listed as income.)
3. I'm two months late on my rent because I needed the money to fix my car.
4. I plan to open a vegetable stand in the market.

## **EVALUATING THE LOAN APPLICATION**

When you evaluate a member's loan application to determine if you should grant the loan, you will be looking for three criteria.

These criteria are referred to as the 5 Cs.

The first of the four Cs is character.

Character refers to the person's willingness to repay the loan.

Is the person motivated to repay?

Does the person understand the obligation to repay?

The second of the 5 Cs is capacity.

Capacity refers to the person's ability to repay the loan.

Is the person capable of repaying?

- Does the person have the resources to repay?

○ The third of the four Cs is Capital.

- Has the member made steady, even if slow, growth in assets or is every penny earned immediately spent?
- The answer will also help determine character.
- Does the member save for the future? Does the member live beyond their means?

- The fourth of the four Cs is condition
  - Circumstances of the economy, industry, CU locale in which the credit is granted.
  - Remember conditions are peripheral circumstances, they are not a basic principle of credit.
- When you evaluate a person's likelihood to repay a loan, you will use both judgment and fact.
  - Evaluating a person's character often involves using judgment.
  - Evaluating a person's capacity and capital to pay involves looking at the member's financial data.
- However, the more factual you can be in evaluating a loan, the fairer you will be.
- Using facts also makes it easier to explain why a member was denied a loan.
  - When you evaluate a member's character, you are evaluating his willingness to repay the loan.
    - How committed is this person to repay the loan?
    - Is the person aware of the obligation to repay?
    - How likely is the person to make this loan a priority in tough times?
  - Let's look at some of the factors you can use in evaluating a person's character.
    - Stability
    - Stability is a good indicator of whether a person will be willing to repay his debt.
    - One way to evaluate stability is to look at how long a person has been on his job or in the same line of business. i.e. farming.
    - As a rule, the longer a person has been at his job, the more likely he is to repay his loan.
    - This is because the member has demonstrated the ability to stick to a situation. Most likely, he has encountered difficult situations on the job, but he has found solutions.
    - This is an indication that he will also likely stick with repaying the loan.
    - Another way to evaluate character is to look at how long he has been at his current address.
    - People who stay at an address have already demonstrated that they are a stable community member.

If they are committed to the community then they will not want to cause embarrassment to themselves by not making loan payments.

Do not automatically assume something is wrong if a member has changed jobs or moved.

During the loan interview it is the loan officer's job to assess the member's situation.

To avoid making rash—and incorrect—conclusions, use stability as only one factor in evaluating a person's character.

## **References**

A member's references can also give you some insight into his character.

Talk to the references. You will learn what they think of the applicant.

If a reference is positive, you can assume that the applicant has a positive relationship with that person.

If a reference tells you the applicant is dependable, you can assume he will also be dependable in repaying the loan.

But if the reference is negative, or is hesitant to talk, or says he doesn't know the applicant well, there may be something wrong.

It may be that the applicant is having trouble finding people who will speak on his behalf.

Or it may be that the applicant has not followed through on past commitments.

The location of a reference also tells you something about the applicant.

If the references are all close, this is an indication that the applicant has formed ties in his community, and will most likely stay there. This also means he is not likely to leave to avoid repaying the loan.

If references are far away, this may be an indication that the applicant has not formed ties in the community. Without ties, the applicant may be more willing to leave town to avoid repaying the loan.

However, be careful about rashly forming conclusions.

There may be a good reason that the reference is far away.

Therefore, if a person's references are far away, plan to ask why, then put the information in context with the other information you collect.

Upon asking, you may discover that a distant reference is a life long friend.

To learn more about an applicant's references, plan to ask questions in the interview.

Ask how the applicant knows the reference. The answer will tell you how familiar the applicant is with his reference. It will also tell you what information you can expect to receive from the reference.

### **Credit history**

You can also learn about an applicant's character by examining his credit history.

Did the applicant have past debt? Was the debt repaid?

Did the applicant pay consistently and on time

Call the utility companies to determine if the borrower has made timely payments on electric and phone bills every month.

If a person has paid bills consistently in the past, it's usually a good indication that he will pay consistently in the future.

On the other hand, a person who has missed payments in the past may be showing that he feels loan repayment isn't important.

### **Past behavior in handling financial difficulty**

Another way to learn about an applicant's character is to look at how they've handled past financial difficulties.

The best way to do this is in the loan interview.

Using a behavioral question, ask the applicant to describe how he has handled tough financial situations in the past.

If he tells you that he cut back on spending, and then stuck with a budget, chances are he will do the same with a new loan.

If he tells you he tried to work out a repayment plan with creditors, that too is positive.

On the other hand, if he dodges your question, or tells you how he was able to dodge his creditors, then he will probably also dodge your credit union during tough times. He is not demonstrating a willingness to repay.

### **Your credit union's past experience with this member.**

A final way to learn about an applicant's character is to review his past experience with your credit union.

Is he a long-standing member? Has he held shares in the credit union?

Has he had previous loans with the credit union? How has he handled repayment?

### **One final reminder**

It is not enough simply to be willing to pay.

A person may be extremely honest and have the highest ethical standards, but if he doesn't have the means to repay his debt, he will eventually be overwhelmed with the debt.

This is why it's also important to examine a person's capacity to repay.

### **Income as it relates to loan amount**

Although income can help you determine whether a member will be able to repay a loan, you can't look at income alone.

You must look at a person's income as it relates to other factors.

First, you should look at income as it relates to the size of the requested loan.

If the loan amount is a small percentage of a person's income, the person is considered more able to pay the loan than if it were a large portion of the person's income.

For example, a person earning \$20,000 a year will probably be seen as able to repay a loan for \$3,000. The loan amount is 15% of the person's income. However, a person earning \$7,000 a year would not be considered able to repay a loan of \$28,000 because the loan is four times the amount of his income.

As you evaluate the loan request, check to ensure that the income and the loan amount are correct. If it appears that the income won't support the loan amount, plan to ask about other sources of income.

### **Income as it relates to expenses**

Another way to evaluate an applicant's ability to pay is to look at a member's monthly expenses as a percentage of their monthly income. This is called *a debt ratio*.

You can calculate a debt ratio by adding all of the applicant's monthly expenses, then dividing them by the applicant's total monthly income.

Expenses include credit card debt, rent or mortgage payments, car payments, and all other payment obligations.

Income includes net income, bonuses, any interest or dividends on shares held in the credit union, and all other incoming monies.

The higher the debt ratio, the less money there is available to repay the loan.

As a rule, a member's debt ratio should not go over 40-50% (if the person's rent or mortgage is included as an expense) and 25-30% (if the member's rent or mortgage is excluded as an expense).

Credit Unions may decide to use a debt ratio as one of the factors to review when evaluating a loan application.

Some will include a member's mortgage or rent as part of the expenses, but allow for a high debt ratio. Others will exclude the mortgage or rent, but opt for a lower ratio.

Other credit unions are willing to allow a higher debt ratio as long as the member has adequate assets to handle emergency situations.

The debt ratio is a much better way to determine a person's ability to repay than is income.

With income, you only know how much a person has coming in.

With debt ratio, you also learn how much of that income is already spoken for.

### **Income as it relates to assets**

Another useful ratio to analyze is the income as it relates to assets.

A person with a high income should be able to accumulate sizeable assets.

If an applicant has a high income, but no assets, this could be an indication that the applicant has difficulty managing money.

For example, let's say a member has been making \$40,000 for three years, but has no assets other than a small amount of shares in the credit union.

Where has this applicant's money gone?

If he has difficulty accumulating assets, will he also have difficulty repaying a loan?

Now let's look at another example. Say a member earns \$8,000 a year, but has been able to save \$3,500 over the past 5 years.

This person is very likely a wise money manager and will easily be able to manage the loan

payment in his budget.

**Two assumptions to avoid**

First, be careful about automatically assuming that a high income equates to a good credit risk. People with high incomes can mismanage money as well as anyone else.

Second, be careful about assuming that a low income equates to a bad credit risk.

Often, people with low salaries are good at managing money because they have to be.

If you look at all the factors when you are evaluating a person's capacity, you will get a good picture of whether or not he is able to repay the loan.

**CASE STUDY—CALCULATING DEBT RATIOS (20 minutes)**

Tell participants that you will read income and debt information for two applicants. Their job will be to: Determine each applicant's debt ratio based on the income and debt. Indicate whether they would consider the debt ratio as a positive or negative factor in evaluating the member's credit request. Here is the information you should provide.

**Applicant #1**

Applicant #1 has the following monthly income.

Net income of \$900.

Share savings interest of \$90.

Total monthly income of \$990.

Applicant #1 has the following monthly debt.

School fees loan of \$50.

Auto loan of \$75.

Assistance to uncle of \$50.

The requested loan amount is \$125.

Total monthly debt would be \$300.

**Calculate the debt ratio for Applicant #1.**

Would this debt ratio have a positive or negative impact in evaluating the member's credit request?

**Applicant #2**

Applicant #2 has the following monthly income.

Net income of \$600.

Share savings interest of \$20.

Total monthly income of \$620.

Applicant #2 has the following monthly debt.

Development loan of \$70.

Auto loan of \$20.

Rent of \$100.

The requested loan amount is \$75.

Total monthly debt would be \$265.

**Calculate the debt ratio for Applicant #2.**

Would this debt ratio have a positive or negative impact in evaluating the member's credit request?

Here are the answers to the case study questions.

**Applicant #1**

Applicant #1's debt ratio is 30% ( $\$300 \div \$990 = 30\%$ ).

The recommended debt ratio is 25-30% when a member's rent is not included as an expense.

Since this member's debt ratio would be at 30%, he is on the high end of acceptable. Therefore, this member's debt ratio would probably be a positive factor in evaluating his credit request.

However, it would be wise to scrutinize other factors relating to this member (character, collateral, other financial ratios), and then evaluate all this information.

### **Applicant #2**

Applicant #2's debt ratio is 43% ( $\$265 \div \$620 = 43\%$ ).

The recommended debt ratio is 40-50% when a member's rent or mortgage is included as an expense.

Since this member's debt ratio would be at 43%, he is well within the acceptable range. Therefore, this member's debt ratio would be a positive factor in evaluating his credit request.

Close the case study by answering student questions.

Present a 10 minute lecture in which you discuss capital.

Create your own lecture, or use the following.

Capital=The financial net worth of the borrower (Assets – Liabilities).

A high capital position indicates ability to absorb possible losses or financial reversals.

If the member experiences a loss of job income are there any resources the member has to continue to repay the loan?

It also is a sign of favorable income and savings patterns in the past, which will likely continue into the future.

When determining a borrower's Capital position look at:

Level of accumulated capital – compared to loan

Growth patterns – recent trends

Savings patterns – look for consistency

Nature and liquidity of the capital

## **6. CONDITION (10 minutes)**

**Conditions refer to the current state of the economy, the employment or business sector of the borrower, and family or social situation.**

Areas to be aware of:

Are there economic indications of a slowdown?

Recession is characterized by falling consumer demand, prices, and profits make it difficult for borrowers to make loan payments

Inflationary times are characterized by rising costs

which lowers profits and repayment ability. Borrowers

who can easily raise prices are better risks than

those who cannot. Small business owners that have the ability to raise inventory prices, are more in control of their businesses profits rather than an agricultural producer that relies on the market to determine price of product. Credit union needs to be aware of these shifts in the economy to make sound loan analysis.

- Will the borrower's business/company be affected?
- What affects will recession and inflation have on the credit union member's income? If the member is a small business owner and recession comes to Azerbaijan, what affects will the recession have on the small business?
- This may require the credit union to visit the member's business to determine what the member/owner of the business is doing to protect the business's profits.
- The credit union loan officer should ask what the member plans on doing to maintain profits, what affects the raising of prices will have on the business's clients? Will the



clients still frequent the store? Will the store allow clients to purchase items on credit? And how will the store ensure that those clients making purchases on credit repay?

- The credit union loan officer from the information obtained would then make a decision of whether to grant the member the loan.
- Are there personal factors that could affect ability to pay?
- It is the loan officer's responsibility to learn all that is possible about their membership. This includes personal information in regards to those members applying for credit.
- Routinely, credit unions operate in a small community, therefore, learning about the member's personal situation is easily done.
- Areas to be aware of: Does the member applying for credit have many dependents. If so, what are their ages and what level of development are the children in? Is the child of school age, which will require money for school tuition, books, clothing? Is the child of marrying age where the family will be required to pay for weddings?
- Also, how are the personal relationships within the family? Does the member owe money to family members? If so, will the family members not request payment on personal loans if the member runs into difficulty with income?
- Is there a high probability of adverse future developments?
- Is the member working at a local factory where it is believed the factory will close in the near future?
- Has the growing season had a lack of rain which will lower crop production at harvest time?
- If any of these situations are evident then they must be discussed with the borrower.
- Loan terms requested within the borrower's application may have to be adjusted based on the conditions faced by the borrower and the market.

## **7. WARNING SIGNS (10 minutes)**

- Warning signs to be aware of when evaluating the loan application:  
Bad credit history-member shows slow pay with other creditors, family members or utility companies
  - Weak personal references-when credit union calls to speak with member identified personal references, references are slow to answer or not willing to speak openly about member.
  - Frequent job changes-member cannot seem to maintain permanent employment.
  - Insufficient payment capacity-member has no additional resources to rely on if main source of income is lost.
  - Inability to verify income-member has no ability to verify to credit union their yearly income. (Note: credit union must define what they will accept as proof of income for all types of employment: agriculture, small business owners, employed by firms, etc.)

Existing delinquent loans

Questionable reputation-member does not hold a sound, trustworthy reputation within the community.

Personal/family problems-member has challenging family relations which cause stress on job performance, ability to repay creditors and maintain economic stability.

Unprofitable business or occupation-member's line of business/occupation is not stable enough to approve loan with sole repayment source as the business/occupation.

If warning signs such as the previous stated occur, credit union must look very carefully as to whether or not to the approve loan.

Once you have considered all four of the Cs in lending—character, capacity, capital and conditions—you are ready to put everything together and look at the entire lending picture.

### **PUTTING IT ALL TOGETHER (15 minutes)**

- Once you have examined all the criteria for the loan request, it is time to look at the big picture.
- Your goal is to identify a pattern. Once you see a pattern, you can decide if the loan should be approved or denied.
- Let's look at some of the patterns you might encounter.
  - The most ideal pattern is one in which you find the member is both willing and able to repay the loan. This person will have an ongoing income, a low debt ratio, some assets, and an established record of paying bills on time.
- Of course, this pattern is an ideal pattern. Let's look at some of the other patterns you might encounter.
- **Watch for the Warning Signs!**
  - **Excessive debt.**
    - A member with a large amount of debt may have trouble repaying a loan.
    - As a rule, if a member's debt is around four times his annual income, he has too much.
    - This is a situation where you should either deny the loan, or find a way to secure it through a guarantor if the other factors in the loan assessment are positive.
  - **Rapidly rising debt.**
    - In this situation, a member experiences a rapid increase in the amount of debt he has.
    - For example, the member has purchased a new auto, bought additional livestock and is financing his child's university education.
    - This person may not have control of his finances.  
Be sure to verify employment/business stability, sources of income and member's capital reserves.

- **High income and no assets.**
  - We have already discussed the problem with a person who has a high income and no assets.
  - It may be a sign that this person is unable to manage money.
  - High-income people should be able to accumulate assets.
- Modest income and strong assets.
  - The corollary to the above situation is the person who, on very little income, can accumulate assets.
  - This is a sign of someone who manages money well.
- Sudden change in lifestyle.
  - If a person has a sudden change in lifestyle, it may be because his financial situation has changed.
  - For example, if a person has recently lost a job, he won't have the income he once had.

If he has recently moved to a better residence, his mortgage or rent may be higher, leaving less discretionary money. There might also be higher maintenance costs.

It is important for loan professionals to identify lifestyle changes and factor them into the loan decision.

#### **A history of financial problems.**

If a member has always had difficulty managing his finances, his behavior will not likely change for a new loan.

When you evaluate the loan application, look for signs that the member has changed his financial management style for the better.

For example, if the member once paid bills inconsistently, but now pays on time, he shows signs of improving his financial management skills.

If you can't find any signs of improvement, consider denying the loan.

As we have seen, each and every one of the four Cs is important in determining whether a member is a good credit risk.

It is not enough simply to be willing or able to repay the loan.

If you use all the tools available to you to evaluate every part of a member's credit record, you will make good loan decisions the majority of the time.

- Facilitate 25-minute case study.
- To facilitate the case study, you can either copy the case study page at the back of this chapter and distribute it to students, or read the case information to students, allowing time after the reading for students to respond.
- To manage your time, allow about 5 minutes to read the information, 10 minutes for participants to determine their answers, and 10 minutes to discuss the answers.
- Tell participants that you will read financial information relating to an applicant. Their job will be to:
  - Determine the applicant's income to loan ratio.
  - Determine the applicant's debt ratio.
  - Determine the applicant's income to asset ratio.
  - Indicate whether they would approve the loan request and explain their answer.
- Here is the information you should provide.
  - The applicant has been at his current residence for ten years.
  - He has been a farmer for fifteen years.
  - He has provided references that are local. Upon checking the references, they were

all positive.

- His house is paid in full.
- He has paid off three previous loans from the credit union.
- He has \$300 worth of shares in the credit union.
- Owns his own farm, farm equipment and livestock valued at \$8000.
- His income is \$10,000 per year net.
- He is requesting a \$1,000 loan to be paid over two years.
- His monthly expenses would be \$600 per month, including his requested loan amount.

- Here are the answers to the case study.
  - The applicant's income to loan ratio is 10% ( $\$1,000 \div \$10,000$ ). This is low, but should not be the sole factor in making the loan decision.
  - The applicant's debt ratio is 72% ( $\$600 \text{ monthly expenses} \div \$833 \text{ monthly income}$ ). This is extremely high. If the applicant had no other assets, this could be a factor in denying the loan. However, since the applicant does have other assets, you may be able to approve the loan with some contingencies.
  - The applicant's income to asset ratio is .03% ( $\$300 \div \$10,000$ ). This indicates that the applicant not a good money manager and cannot save a significant amount of his earnings.
- If you look strictly at the applicant's capacity to pay, you might deny him the loan.
- However, the applicant has strong character.
- He has physical assets that are lien free.
- His references are good.
- He has already repaid three loans.
- He is consistent and on time in paying all of his utilities.
- He is stable both at his business and at his residence
- Under these circumstances, the applicant is probably a good credit risk.
- If you wanted to make the loan extremely safe, you could ask the applicant to use some of his share savings as security for the loan.
- Close the case study by answering student questions.

### CASE STUDY—CALCULATING DEBT RATIOS

One way to determine a person's ability to repay a loan is to analyze his debt ratio. Follow are summaries of two applicants' income and expenses. For each applicant, do the following.

- Determine the applicant's debt ratio.
- Indicate whether you would consider the debt ratio as a positive or negative factor in evaluating the member's credit request.

<b>Applicant #1</b> <i>Monthly Income</i> Net income:	\$900	<b>Applicant #2</b> <i>Monthly Income</i> Net income:	\$400
<b>Total:</b>	<b>\$900</b>	<b>Total:</b>	<b>\$400</b>
<i>Monthly Debt</i>		<i>Monthly Debt</i>	
Assistance to uncle:	\$50	Rent:	\$100
Requested loan amount:	\$125	Requested loan amount:	\$150
<b>Total:</b>	<b>\$175</b>	<b>Total:</b>	<b>\$250</b>

Debt ratio:		Debt ratio:	
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Positive or negative impact in evaluating the member's credit request?

## REVIEW OF SPECIFIC LOAN FORMS AND LENDING PROCEDURES

- The loan application process
- Working Capital Loans
- Investment Credit Loans
- Loan Denial
- Disbursement
- Write comments and critical points you want to make in the margins of this Instructor's Guide.

### Step By Step Lending Process with Accompanying Forms (50 Minutes)

Forms need to be available for participants to review during lecture.

Create your own lecture, or use the following.

By now you are all fully equipped to become loan approval specialists! We have reviewed all areas of the credit administration process. Now it is time to bring our training to specifics as used within the credit unions.

#### Lending Process

The following is a step by step process to guide a loan officer in completing the application, forwarding to credit committee for their review and recommendation to the board of directors, and finally board of directors review and determination of loan. All forms associated with the lending process are available in handouts as a part of this manual.

There are two types of loan products offered by the credit unions

(Note: For full description of loan products please see CU Credit Administration Manual Policy and Procedures):

- Working Capital Loans
- Investment Credit Loans
- The following reflects the credit administration process and corresponding required form for each type of loan product:
  - Working Capital Loans
  - The loan process will start with a loan request from the potential borrower. The loan request is to be made in person at the CU.
  - The borrower will be given a Loan Application Form and Business Plan for Short Term Credits (**Form 1**) and
  - A written list that details what the borrower needs to provide, Information needed from Potential Borrowers (**Form 2**) so that the request can be processed promptly.
  - All loan requests must be in writing on the approved loan forms and given to the Credit Union Loan Officer.
  - The application should be completely filled out by the member and if needed the Regional Representative may assist. The more information the borrower provides the credit union, the easier it will be to collect the loan, if the loan becomes delinquent.

- The application should be completely filled out by the member and if needed the Regional Representative may assist. The more information the borrower provides the credit union, the easier it will be to collect the loan, if the loan becomes delinquent.
- For all approved secured loans, there will be proof of insurance (if available), collateral value and condition, Information on Collateral Determination Form **(Form )** along with a security agreement or proof that the lien on the security has been filed with the proper authorities and that the CU has “clear title” should the collateral have to be repossessed. (Note: at this time credit unions are not holding physical instruments as collateral for their credit union member loans.)
- If the borrower is self employed it is often difficult to verify their income. The CU Loan Officer will have to review the member’s cash flow by analyzing Loan Application and Business Plan Form, accounting records such as accounts receivables, etc. or if this is not available then invoices, price lists, volume of daily transactions, bank account statements, talking to vendors who have a similar business and asking them about how much they make and what they think the potential borrower might make.
- Before proceeding to the analysis of the submitted application, the loan officer should verify all the references contained in the application (personal and credit).
- Once all of the necessary information has been obtained the completed loan request will be given to the credit committee to make the loan proposal.
- Every member submitting a loan application will have an interview with the credit committee, or board.
- After credit committee makes analysis of the loan the Credit Committee Proposal to the Board of Directors **(Form 5)** must be completed, all credit committee members must sign the proposal.
- Board of Directors review proposal from Credit Committee and make determination of credit by completing Decision of Board of Directors **(Form )**.

## **2. Investment Credit Loans**

- Follow same loan documentation and approval procedures as stated previously, but using Loan Application Form and Business Plan for Investment Credits **(Form .)**.

## **3. Line of Credit Loans**

- Follow same loan documentation procedures as stated previously using Loan Application Form and Business Plan for Investment Credits.

## **4. Loan Denial Guidelines**

- It is management and the official’s responsibility to use the member share deposits wisely therefore certain loan requests should be denied when:
  - Member has a bad credit history;
  - Insufficient payment capacity to repay the loan in its entirety;
  - Inability to verify the borrower’s income;
  - Current delinquent loans or previous obligations to CU has not yet been paid;
  - Value of the collateral is insufficient for the loan request;

Members that have caused the CU or another financial institution a loss;  
Members that have a questionable reputation;  
Members with personal and/or family problems;  
Unprofitable business or occupation;  
Members who do not want or can not disclose information about  
their financial status or they do not have adequate references;  
Loans to finance interest on existing debts; and  
Collaterals in which the property does not have clear title.

The member will be informed in writing of all loan denials by the loan officer based on the recommendation of the credit committee and final decision by the board of directors.

The reason for the denial will be specifically addressed within the written loan denial form.

The written denial notice is to be delivered to the member within 7 business days from the denial decision.

## **5. Loan Disbursement**

If the credit committee and board of directors have both signed for approval of loan, it is time to begin the disbursement process.

The following is the procedures and forms required:

At time of loan disbursement both loan applicant and guarantor come to the credit union and the borrower signs the Collateral Contract for CU Members **(Form .)**, and

The guarantor signs Guarantor Contract for CU Members **(Form .)**.

If member has been approved for a Line of Credit Loan, then Credit Contract for CU Members must be completed and signed. **(Form ...)**.

Subsequent Advances will be made upon request by the member after completing the appropriate form, Additional Credit Contract for CU Members. **(Form)**.

*The initial approval of the loan does not guarantee that the member will be given funds whenever they want. The CU can deny additional requests based on poor past payment, not paying the loan balance down to an acceptable level, or new information gathered about the borrower that indicates the borrower will be unable to pay the higher loan balance. At each loan request the credit committee can verify the borrower's creditworthiness, capacity to repay, and collateral value (if applicable) if they choose and make the decision whether or not to approve the advance.*

- Under no circumstances may anyone involved in the loan approval process be allowed to disburse the loan proceeds to the borrower or be involved in the collection process should the loan become delinquent.
- The Payment Order **(Form ..)** is completed by the credit union accountant and forwarded to teller for cash funds.
- Cashier counts loan proceeds out to member and the member signs Receipt Order **(Form ...)** to be used as record that member has indeed received disbursement funds
- Member Credit Account **(Form ...)** is completed by the accountant and maintained as record for the credit union as to number and type of credit disbursed to members.
- Loan Officer inputs all loan information on credit union software and files completed file in fire proof file cabinet.
- Interest Accrual **(Form ..)** is used by Accountant to record interest accruals throughout the payment of the loan.

## **CONTROLLING LOAN DELINQUENCY**

- Define delinquency.
  - Recognize the importance of controlling delinquency.
  - Identify the causes of delinquency.
  - Identify the types of delinquents.
  - Identify delinquency classifications.
  - Use the loan application process to prevent delinquency.
  - Prepare delinquency policy.
  - Create a system for monitoring and collecting delinquent loans.
  - Distinguish between the different delinquency notices and use them appropriately.
  - Negotiate with delinquent members.
  - Provide appropriate financial counseling to delinquent members.
  - Take last resort actions if necessary.
  - Recognize the communications skills needed for working with delinquent members.
  - Prepare and analyze a delinquency report.
- 

## KEY TERMS AND CONCEPTS

- Definition of delinquency
- Importance of delinquency control
- Causes of delinquency
- Types of delinquency
- Delinquency classifications
- Steps for preventing delinquency
- Delinquency policy
- System for monitoring and collecting delinquent loans
- Delinquency methods
- Negotiating with delinquent members
- Financial counseling
- Communication skills
- Delinquency report

You will be presenting the following topics, so manage your time wisely.

- Definition of delinquency
- Why it's important to control delinquency
- Causes of delinquency
- Types of delinquents
- Delinquency classifications

A loan delinquency is caused when a member stops paying his loan according to its terms.

- A delinquent loan is defined as any loan in which the full payment has not been received per the loan contract.
- Depending on the payment schedule the payment could be all of the principal and interest due, monthly interest only payments, or the monthly principal and interest payment(s).

Credit unions rely on their members to pay their loans on time.

- An excessive number of delinquencies can put a credit union in bad financial condition.
- Therefore, it is important to control delinquency.

There are a number of reasons that members become delinquent.

Circumstances-Loss of a job, death in the family or unexpected hardship.



Intellect-Poor financial planners-they spend more than they earn.

Emotion-Hostile or defensive members with a “score to settle”.

Some members may simply be dishonest.

There are three types of delinquents.

### 1. The sudden non-paying member

- This is a member who is consistently on time with his payments.
- Then there is a sudden and major reason for his delinquency.
- Usually the reason is beyond the member’s control.
- Members in this category are the most likely to notify the credit union of their problems so that they can work out a repayment schedule.
- Generally, this member wants to pay his loan, but he is in a bad financial situation.
- It is worthwhile to work with these members and give them relief.
- Once they are back on their feet, they will become loyal members in good standing.
- To help this member the credit union may decide to offer a loan refinancing.
- Loan refinancing occurs when the CU gives a debtor **new payment conditions** different from the ones originally stipulated within the loan contract. This is because the debtor cannot make the payments in a timely fashion, according to the **original terms**.
- **The conditions necessary to approve a loan refinancing are such that there is a permanent change in the basis on which the loan was granted.** Examples are:
  - loss of a crop or reduction in income due to a job change.
- Loan Refinance Approval:
  - All loan refinances are to be approved by the credit committee and board. CU employees have no authority to approve a loan refinance.
- In order to grant a loan refinance the following is to be complied with: Whatever caused the borrower to have trouble **in making the loan payments has been changed or solved. For example - if the member lost their job, they must have a new one before a loan refinance can be granted.**
  - Three full monthly payments or 3 payments at an agreed upon (between the credit committee and board and the borrower). The agreed upon reduced payment are to be made prior to any loan refinance.
  - This is important; it demonstrates the borrower’s desire to repay the loan.
  - All interest has to be paid current. (No refinancing of overdue loan interest is allowed.)
  - Under no circumstances should the interest be added to the principal balance when the loan is refinanced.
- If the loan was guaranteed by another individual, the guarantor shall also sign the refinanced loan, and shall be notified when an agreement for payments different from the original terms is reached.

The debtor must present all the documents required for a new loan to the loan officer, the loan officer will

### **The occasional non-paying member**

This is a member who is late with a payment once in awhile.

He may have been out of town when the loan was due, or he may have become very busy.

Whatever the reason for his occasional lateness, he usually responds to reminder notices.

### **The chronic non-paying member**

This is a member who makes a habit of being late with his payments.

- He also lets his payments lapse for long periods of time.
- Even if he brings his loan up-to-date, he is likely to let it lapse again.

- Some of these members are careless and don't realize what they are doing to their credit history.
- Others are knowingly trying to work the system to get out of repaying the loan.
- Whatever the reason, chronic non-payers are expensive to the credit union.
- They require constant monitoring and follow up, which uses valuable credit union resources.
- Many credit unions will classify their loans into different categories. Here are some of the more common categories.
  - **Late account**
    - This is an account where the member misses a single payment.
    - Usually, the member will repay when reminded. This is also known as the "first notice account".
  - **Slow account**
    - This is an account that is twenty days or more past due, and the member has not responded to notices.
    - Collection action most likely has already been taken on this account
    - It is important to learn why the member is so late with the loan.
    - Maybe the solution is simple. For example, maybe the due date is inconvenient and, if the credit union changes it, the problem will be solved.
    - A slow account is not yet in serious trouble, and the credit union should make every effort to prevent further delinquency.
  - **Chronic slow account**
    - This is an account that is constantly past due.
    - An account in this category needs persistent and firm follow-up communication.
  - **Skip**
  - This is a member with a delinquent account who has left town without leaving a forwarding address.
  - Some members skip on purpose, knowing that they have no intention to repay the loan.
  - The most important action in dealing with a skip is to locate him.
  - Once he is found, make sure all the credit union records are updated.
  - Then, stay in constant contact until payment is resumed.
  - **Loss**
  - This is an account that is almost impossible to collect.
  - In some instances, the board of directors will recommend writing it off.
  - Even so, the loan professional should continue efforts to recoup the money from a loss account.
  - Sometimes, a member's financial situation will improve, and payment can resume.

## Effects of Delinquency on the Credit Union

### Results of High Delinquency...

- Slows the build up of Institutional Capital
- Lessens the credit unions ability to provide services members want and need

- Results in credit rationing
- Lowers liquidity
- Diminishes the ability to provide for credit union operational costs including staff wages

You have just learned a variety of facts relating to loan delinquency. Tomorrow, you will do a case study that will have you identify types of delinquencies.

### **CASE STUDY—IDENTIFYING DELINQUENCY TYPE (20 minutes)**

- To facilitate the case study, you can either copy the case study page at the back of this chapter and distribute it to students, or read the cases to students, allowing them time to respond.
- To manage the time, allow about 10 minutes for reading and answering the cases, and 10 minutes for discussing the solutions.
- Tell participants that you will read four case descriptions to them. Their job is to identify which of the following types of delinquency each case is.
  - Circumstance
  - Lack of understanding
  - Irresponsibility
  - Dishonesty
- **Case #1:** A member has not paid on his loan for three months. When you call him about it, he tells you he has forgotten the payment amount.
- **Case #2:** A member hasn't paid on his loan for four months. Every time you call, he has a different excuse. Today when you called, you caught him in a lie. He told you his mother was ill, but last month when you called, he told you his mother died.
- **Case #3:** A member misses one payment and calls you to say his son lost a leg in an accident.
- **Case #4:** A member misses one payment, but this is the fifth time this has happened in less than a year. When you call the person to talk about it, he tells you he didn't know the deadline was so hard and firm. He had always assumed that as long as he paid within a couple of months, it was fine.
- **Here are some possible solutions to the cases.**
  - **Case #1:** A member has not paid on his loan for three months. When you call him about it, he tells you he has forgotten the loan payment amount.
  - **Solution:** This member is irresponsible and shows it by not paying the Credit Union loan and also by not contacting CU if he did indeed forget the loan payment amount.
  - **Case #2:** A member hasn't paid on his loan for four months. Every time you call, he has a different excuse. Today when you called, you caught him in a lie. He told you his mother was ill, but last month when you called, he told you his mother died.
    - **Solution:** This member is dishonest and is probably trying to get out of paying the loan altogether.
  - **Case #3:** A member misses one payment and calls you to say his son lost a leg in an accident.
    - **Solution:** This member is a victim of circumstance and should be allowed time to adjust to his new circumstances.
  - **Case #4:** A member misses one payment, but this is the fifth time this has happened in less than a year. When you call the person to talk about it, he tells you he didn't know the deadline was so hard and firm. He had always assumed that as long as he paid within a couple of months, it was fine.
    - **Solution:** The member lacks understanding of the terms of the loan. Take the time to

reacquaint him with his obligations.

- Once you have reviewed all four cases and their solutions, use any remaining time to answer student questions.

### **3. PREVENTING DELINQUENCY (30 minutes)**

The importance of preventing delinquency.

Using the loan application process to prevent delinquency.

Having a delinquency policy.

Having a system for monitoring and collecting delinquent loans.

Create your own lecture, or use the following.

Statistics have shown that, the older a loan gets, the more trouble a credit union will have recovering it.

#### **Delinquency Recovery Rates:**

Past Due in Days	Recovery Rate
30 days	95%
60 days	89%
90 days	80%
120 days	70%
240 days	50%
360 days	10%

- Therefore, it is important for a credit union to have policies and procedures aimed at preventing delinquency.
- An obvious, but important, way to prevent delinquency is to execute the loan application process completely and accurately. When you do this, you ensure:
  - That only members who demonstrate repayment ability get loans in the first place.
  - That the application contains complete name and address information in case you need to reach the applicant at a later date.
  - That the credit union has complete names and addresses of employers and references in case you need to reach them to locate the applicant.
  - That the member was told about his repayment obligations during the loan closing.
  - That all the important loan documents (the contract, collateral agreement, guarantor statement) were completed and signed at the loan closing.
- Another item that helps prevent delinquency is a delinquency policy.
- The delinquency policy is followed to cover all aspects of credit union policy and procedures for loans that have become delinquent. (Note: Credit Union Delinquency Policy and Procedures provided as a handout)
- It is up to the loan professional to follow the policy.
- However, the best policy in the world will won't help if the credit union doesn't have a system for monitoring and collecting loans that do become delinquent.
- Whether the system you establish is computerized or manual, it must do the following things.
  - Flag delinquent accounts on a daily basis.
  - Identify how late each delinquent loan is.

- Promptly generate the appropriate follow-up action.
- Generate appropriate follow-up communication.
- Document follow-up status.
- Suspend action if payment is received.
- Document payment promises made by members.
- Follow-up on payment promises made by members.
- Refer delinquent loans elsewhere for more aggressive collection.
- Charge off the loan when it is appropriate to do so.
- Document all delinquency activity, so that the credit union can monitor delinquency trends and make adjustments in policy.
- Now that we have talked about the techniques for preventing delinquency, we'll be doing a case study relating to delinquency policy.

#### **4. CASE STUDY—DELINQUENCY POLICY (20 minutes)**

Facilitate a 20 minute case study in which students will review the Model Credit Union Delinquency Policy and Procedures.

To manage your time, allow about 10 minutes for reading and answering the questions, and 10 minutes to discuss the answers.

Ask groups of students to work together. Have them assume that they are all on a credit committee and that they have been asked by the board to review the delinquency policy.

While reviewing the policy they need to see if the policy addresses the following questions:

- How will the credit union learn about missed payments?
- Who should contact the delinquent member?
- How soon after missing a payment should a member be contacted?
- How soon and how frequently after the first contact should the member be contacted again?
- What method should the credit union use for making these contacts?
- Payment reminder form?
- Personal letter?
- Phone call?
- At what point should a delinquency be turned over to a higher authority?
- Who should the higher authority be?

#### **5. DELINQUENCY CONTACT METHODS (30 minutes)**

- When a loan professional follows his credit union's delinquency policy, he will most likely be asked to send out delinquency notices, make telephone calls and begin judicial procedures.
- The credit union must be flexible in its methods of contacting delinquent borrowers. The Delinquency Policy provides guidelines, but those guidelines may be adjusted for cases that are more difficult or require additional attention.
- The key is to keep constant contact with delinquent borrowers to try and obtain payment.
- An individual collection card must be opened for each delinquent borrower. (See Delinquent Borrower Collection Card within the Collection Policy, Appendix 6)
- All contact information with the borrower and the guarantor in the form of collection letters, member visits to the Credit Union, Credit Union visits to the member, and telephone conversations, as well as judicial procedures must be documented as to dates that the activity has taken place, and agreements made with the delinquent borrower.
- The collection card will be used to keep track of the progress of the collection activity

and will act as a prompting notice to the credit union staff persons responsible for collections.

- Let's examine the various types of delinquency methods and when to use them.

### **Types of Delinquency Contact Methods.**

#### Use of collection letters

- Effective collection letters use appeals that are graded in strength and tone of insistence as delinquency progresses.
- As delinquency progresses, accounts usually call for individual attention.
- The loan officer may sign the first collection notice.
- If delinquency persists the Manager of the credit union, credit committee members or board of directors, may sign the corresponding collection letters.
- Again, the most important aspect of delinquency contact is to continually be in communication with the delinquent borrower.

#### • Using the telephone for collections

- Telephoning is one of the best forms of collection activity.
- It is one of the most efficient and effective ways to collect money.
- Maximum past-due accounts can be covered.
- Reduces the cost-per-account contacted and collected.
- The best way to understand a debtor's situation and to resolve the situation.
- Be sure when you contact the borrower you listen to what they say and write down the conversation held with the borrower on their individual collection card.
- While on the phone, negotiate a date and amount the member will be making payment to the CU.
- The credit union staff person must note on a calendar that the member has made a commitment to pay the credit union and for what amount.
- On that date, the credit union staff person must follow up to see that the member has made payment.
- If the member has not made payment, then the credit union must contact the member again, by phone call or personal visit, to determine why the promise to pay was not upheld.
- If the member continues to break promises of repayment to the credit union, it may be time for the credit union board of directors to determine what further action to collect the loan should be.

#### Judicial collections

- Legal actions should be the last resort of the credit union that has worked their delinquency accounts to the point of "diminishing returns" or have little hope of collecting past due payments.
- Legal action is costly and a time consuming activity.
- Collect from Guarantors
  - Guarantors have equal financial obligations to the credit union as the borrower. If the borrower does not pay, Guarantors must pay.
  - Copies of all correspondence with borrowers needs to be copied to Guarantors.
  - Phone calls must be made to Guarantors as well to inform them of the delinquency and the requirement of the guarantor or borrower to pay.
  - Inform the guarantor that they may be taken to court for collection procedures if payment is not made on the loan.
  - **Guarantors must:**

Be in better financial position than borrower

Be educated as to their responsibilities

Understand that guaranteeing a loan may disqualify them from receiving loans themselves

Be contacted at the first sign of delinquency

They should receive all notices and phone calls that the borrower does.

CU must have MIS in place to monitor Guarantors

## **6. DELINQUENCY CONTACT TIMETABLE (20 minutes)**

Delinquency management and control has the following recommended timetable to follow in order to contact delinquent borrowers:

When the borrower's payment is 7 days late the first collection notice (See appendix-- shall be sent and phone contact or personal visit attempted.

The second contact (See appendix ---) is made after 15 days.

If a phone or personal contact was not made with the first notice, it should be made no later than the second notice or 15 days delinquent.

The third notice (See appendix 5) is sent and a personal contact is to be made after there has been no payment in ..... days.

If these initial measures do not obtain the desired results the CU must decide what action to take next with the borrower.

Will the credit union proceed collecting the debt through the judicial process? This must be the last alternative.

The collection process is one that can be adjusted according to the degree of delinquency of the borrower.

The collector must rely on information in regards to his borrower and the anticipated recoverability of the loan.

If the collector realizes the loan recovery rate is very low, in other words, there is not much hope the loan will be repaid by the borrower, than the loan collector may proceed with judicial proceedings right away.

### **Collection Tips... How do you ask members to Pay?**

- Stay calm-ignore the fight or flight instinct. Never refuse to listen.
- Listen- Do not interrupt. Give them a chance to explain.
- Show understanding. Let them know you can identify with the situation.
- Identify the problem. Make sure you understand their situation.
- Find some solution. Come up with a compromise.
- Keep smiling. Keep your mood positive.
- Hand them a sheet that says don't pay more than you need to...if you don't pay, this is what it will cost you...in delinquent charges...the sheet should have their name, account number, opening balance of the loan, amount due, and the amount of their monthly payments.
- Continue to use collection letters
- Continuous Collection visits
- The credit union should be seen as a helper and not the problem.
- Collectors are the "good guys", the CU is there to help the members
- Visit continually - same strategy --- be polite and friendly.

## **7. FACE TO FACE MEETINGS WITH DELINQUENT MEMBERS (15 minutes)**

- When the loan professional meets with a member, there are important steps he should follow.
  - **Step 1:** Schedule a face-to-face meeting.
    - Discussions to repayment can't be conducted effectively over the phone.
    - It is important for each party to see the other person's non-verbal communication.
    - Sometimes the member will agree to come to the credit union, or the credit union may be lucky and have the member come to the credit union on their own decision.
    - When a visit to the credit union is not possible, then credit union staff or a designated credit union representative (Credit Committee or Board of Director member) may have to visit the member at their place of visit or home.
    - Also, both parties need to sign the agreement they reach.
  - **Step 2:** When a meeting is scheduled at the credit union, start the meeting by creating a positive environment for working.
    - Offer refreshments.
    - The loan professional should summarize his objective for meeting: he wants to help the member honor his loan commitment.
    - When a meeting is needed at the member's residence it is best to determine a time when the member is most likely to be at home.
      - The credit union representative should first state the reason for the visit-non payment of the credit union loan.
      - Begin by asking why the member has chosen not to pay the loan.
      - Discuss the repercussions of non payment to the member: higher costs in penalty fees, possibility of being taken to court and the requirement of paying all associated court costs.
      - The credit union representative should be firm, but polite.
  - Same applies for a visit to the member's workplace.
  - Determine a time when the member is most likely to be at work: first thing in the morning, right after lunch.
  - The credit union representative must be polite, but firm in discussing the member's delinquency with the borrower.
  - Care should be taken by the credit union representative while holding this discussion to make sure the conversation is held in a private place out of the reach of others being able to overhear.
  - Same discussions regarding the delinquency and the need for reaching an agreement should be obtained.
  - In all cases, the credit union representative needs to inform the borrower that visits to home and business will continue until loan is paid current by the borrower or guarantor.

**Step 3:** Get the member's agreement to work for a solution.

**Step 4:** Ask the member to lay out his financial situation.

**Step 5:** Ask the member what steps he is willing to take to improve his financial situation.

Get a second job?

Borrow money from a friend or relative?

Cut back on certain expenses?

Go to financial counseling?



**Step 6:** Be prepared to communicate what the credit union is willing to do.

- **Will the credit union provide further credit services if the loan is brought current and remains current for the remainder of the contract?**
- **Explain to the borrower if the delinquency continues no further credits will be provided to the member by the credit union.**

Step 7: Find a solution that is acceptable to both the member and the credit union.

Step 8: Summarize the agreement in writing.

Step 9: Get the member to sign the agreement.

Step 10: Compliment the member for working hard to correct the situation under such difficult circumstances.

Meeting with delinquent members is never easy, but when a credit union discusses repayments with the borrower effectively, the borrower will have more incentive to repay the loan.

#### **PROVIDING FINANCIAL COUNSELING (10 minutes)**

- Sometimes a member will agree to go to financial counseling to learn how to manage his money.
- Depending on the credit union, the loan professional may do the counseling, or one of the official family members of the credit union.
- Regardless of who does it, here is what a member can expect from financial counseling.
  - The planner will help him set financial goals.
  - He will be asked to summarize his income and expenses.
  - He will be asked to identify areas where his expenses could be reduced.
  - He will be asked to identify areas where he might be able to earn extra income.
  - He will be asked to list his assets.
  - He will be asked if he can use any of the assets to reduce his debt.
  - The planner will help him set up a budget.
  - He will learn to control unnecessary spending.
  - Ultimately, he will learn the principles of sound financial management.

#### **9. LAST RESORT ACTIONS (5 minutes)**

- We learned that it is important to tell the member what will happen if he doesn't pay his loan.
- When a credit union has worked without success to get a member to pay, it must follow through on those actions.
- **Let's review them now.**
  - Write a letter to the member informing him that the credit union is declaring his loan in default, and outlining the actions the credit union will be taking.
  - Inform the member that he will be responsible for all loan principal, interest and late penalties, plus court costs if necessary.
  - If the loan had a cosigner, contact him to inform him of his obligation to pay the defaulted loan.

## 10. CASE STUDY—HANDLING DELINQUENCY (30 minutes)

Facilitate a 30 minute case study.

To facilitate the case study, read the following cases to students, allowing them time to respond.

To manage the time, allow about 15 minutes for reading and answering the case problems, and 15 minutes to discuss the solutions.

Tell students that you will read two case descriptions to them. Their job is to determine the next action that should be taken on each.

- **Case #1:** Over the years, a credit union member has had several loans and has always repaid them promptly. Four months ago, he took out a loan for livestock. He made the first two payments, and then suddenly stopped. The credit union has sent him two reminder notices, but has received no response. What is the next step?
- **Case #2:** A year ago, a new member took out a loan to cover his only son's school expenses. He paid promptly for eight months, and then stopped. The credit union sent out reminder notices, and then made several unsuccessful attempts to call the member. Finally, the credit union called a reference to see if he knew the member's location. The reference explained that the member's son had died, and the member moved away. What is the next step?
- **Here are some possible solutions to the cases.**

**Case #1:** Over the years, a credit union member has had several loans and has always repaid them promptly. Four months ago, he took out a loan for livestock. He made the first two payments, and then suddenly stopped. The credit union has sent him two reminder notices, but has received no response. What is the next step?

**Solution:** The credit union should try to make telephone contact. This is a member who is normally very dutiful in repaying loans. Something could be terribly wrong. If the member is in a difficult financial position, the credit union should try to work with him.

**Case #2:** A year ago, a new member took out a loan to cover his only son's school expenses. He paid promptly for eight months, and then stopped. The credit union sent out reminder notices, and then made several unsuccessful attempts to call the member. Finally, the credit union called a reference to see if he knew the member's location. The reference explained that the member's son had died, and the member moved away. What is the next step?

**Solution:** The credit union should get as much information as possible from the reference. Where did the member move? What is his new address? Is there a phone number? Are there any relatives who might have information about this person? Once the member is located, he should be contacted by telephone if possible. Since the member paid consistently prior to his son's death, he may be under the mistaken notion that he is not required to pay the loan once the son is dead. Explain the member's obligations to repay the loan, and then get him to commit to resuming payments. Once you have reviewed both cases and their solutions, use any remaining time to answer student questions.

## 11. COMMUNICATIONS SKILLS (20 minutes) *Optional Activity*

On the one hand, they are members, so you want to treat them with the respect and dignity they deserve.

Let's form into small groups and identify the communications skills necessary for handling delinquent members.

- Break the large group into smaller groups of 4-6 people each.
- Allow the groups 10 minutes to identify as many communications skills as they can.
- When the discussion time is up, bring the small groups back together into a large group.
- Allow 10 minutes for them to share their answers, and then add those that you feel are important.
- The students will come up with many responses. Following are some of the most important.
  - **Ability to inspire trust**—the member will be willing to discuss his situation only if he trusts the loan professional.
  - **Listening skills**—the loan professional must be willing to give his undivided attention to the member. Otherwise, he will not be able to understand the member's situation.
  - **Ability to draw the member out**—the loan professional must know which questions to ask to get the member to talk.
  - **Ability to empathize**—the loan professional must be able to understand the member's situation in order to work with it effectively.
    - **“Non-judgmental”**—the loan professional can't look down upon the member or act in disdain over his difficult financial status.
    - **Willing to work with the member's problems**—the loan professional needs to handle the member's financial problems as though they were his own.
    - **Firm, but tactful**—the loan professional needs to be very clear about the member's obligation, but also needs to communicate it without sounding harsh.
    - **Facilitative**—the loan professional needs to be able to lead the member through the problem-solving process.
    - **Positive thinker**—the loan professional needs to assume that the member wants to pay the loan and clean up his financial record.
- Close the discussion by thanking students for their participation and reminding them to use these skills the next time they find themselves working with a delinquent member.

### **ANALYZING DELINQUENCY REPORTS (20 minutes)**

- To be able to do this, the credit union must maintain a variety of data relating to delinquency.
- An efficient way to maintain this data is to compile it into a delinquency report, which shows the delinquency ratios of all the different loans offered by the credit union. (Model Credit Union Collections Policy, Appendix 7)
- To make sure this happens, someone in the credit union should be specifically responsible for compiling and analyzing these reports.
  - It might be someone on the credit committee.
  - It could be a loan professional.
- To determine a delinquency ratio, simply take the total number of delinquent loans and divide it by the total number of loans in the credit union.
- A delinquency ratio should be calculated using **all** of the credit union's loans, but there should also be individual delinquency ratios for each category of loan.
  - Working Capital loans
  - Investment Credit loans
  - Loans to Credit Union Officials and Staff
  - Loans to inexperienced borrowers
  - Loans to unstable borrowers
- By consistently producing a delinquency report, the credit union can measure its

performance in managing delinquency.

- Here are some of the things you can learn from a delinquency report
  - Is one category of loan more likely to be delinquent than another?
  - Has there been a significant increase in delinquencies in a given category?
  - If yes, is there something that can be changed to make this category perform better?
  - If yes, does that category's delinquency ratio improve after the change is implemented?
  - Is there a type of loan where the delinquency ratio is so bad that the credit union should consider no longer offering the loan?
  - How is the credit union's delinquency ratio overall? A score of 5% or below is considered ideal.
  - A score of 10% or below is considered acceptable.
  - A score of 10-20% indicates problems. It is time to assess loans getting these ratios.
  - A score of over 20% indicates serious problems. The credit union may be in financial trouble.
  - How do individual loan ratios compare to the overall credit union ratio?
  - Which loan categories perform better than average?
  - Which loan categories perform below average?
- One might argue that loan delinquency is a part of doing business. Although this is true, a credit union can control its delinquency by maintaining and using a delinquency report

### **CASE STUDY—ANALYZING A DELINQUENCY REPORT (30 minutes)**

- Read (or show) the case study data to the students.
- Tell them that their job is to study the data, and then write down their conclusions.
- To get the students started, you may want to generate one or two conclusions as a large group.
- Then, once students appear to understand the project, encourage them to work in their groups.
  - When time is up, call the small groups back together and lead a discussion.
    - Ask students to share the conclusions they formed.
    - Add any that you feel are important.
- The students will come up with many conclusions. Following is a list of some of them.
  - The credit union's delinquency ratio is acceptable, but not ideal.
  - With one exception, all delinquency ratios spiked from January to February. It might be worthwhile to analyze if there was an unusual problem or occurrence that month.
  - Working Capital loans are consistently higher than the credit union's average. Perhaps it would be worthwhile to examine the policies and procedures used for granting Working Capital loans.
  - First-time loans have a good ratio. Perhaps it would pay to analyze the policies and procedures used for granting these loans, and then consider adopting them to Working Capital loans.
- Once all students have had a chance to share their conclusions, use any remaining time to answer their questions.

the following delinquency report and write down your conclusions.

### First Quarter Delinquency Ratios

Type of Loan	January	February	March
Working Capital loans	9.7%	9.9%	10.3%
Investment Credit loans	4.1%	4.0%	4.3%
Collateral loans	4.6%	4.9%	5.0%
First-time loans	8.3%	8.6%	7.9%
<b>Total credit union Loans</b>	<b>7.7%</b>	<b>8.1%</b>	<b>8.1%</b>

Conclusions

### CASE STUDY—HANDLING DELINQUENCY (30 minutes)

#### Case Study

- Facilitate a 30 minute case study.
- To facilitate the case study, read the following cases to Participants, allowing them time to respond.

### CHAPTER 8: CONTROLLING LOAN DELINQUENCY

#### Case Study “continued”

To manage the time, allow about 15 minutes for reading and answering the case problems, and 15 minutes to discuss the solutions.
Tell Participants that you will read two case descriptions to them. Their job is to determine the next action that should be taken on each.
<b>Case #1:</b> Over the years, a credit union member has had several loans and has always repaid them promptly. Four months ago, he took out a loan for livestock. He made the first two payments, and then suddenly stopped. The credit union has sent him two reminder notices, but has received no response. What is the next step?
<b>Case #2:</b> A year ago, a new member took out a loan to cover his only son’s school expenses. He paid promptly for eight months, and then stopped. The credit union sent out reminder notices, and then made several unsuccessful attempts to call the member. Finally, the credit union called a reference to see if he knew the member’s location. The reference explained that the member’s son had died, and the member moved away. What is the next step?
15 minutes to discuss the solutions.

#### Here are some possible solutions to the cases.

**Case #1:** Over the years, a credit union member has had several loans and has always repaid them promptly. Four months ago, he took out a loan for livestock. He made the first two payments, and then suddenly stopped. The credit union has sent him two reminder notices, but has received no response. What is the next step?

**Solution:** The credit union should try to make telephone contact. This is a member who is normally very dutiful in repaying loans. Something could be terribly wrong. If the member is in a difficult financial position, the credit union should try to work with him

**Case #2:** A year ago, a new member took out a loan to cover his only son’s school expenses. He paid promptly for eight months, and then stopped. The credit union sent out reminder notices, and then made several unsuccessful attempts to call the member. Finally, the credit union called a

reference to see if he knew the member's location. The reference explained that the member's son had died, and the member moved away. What is the next step?

**Solution:** The credit union should get as much information as possible from the reference. Where did the member move? What is his new address? Is there a phone number? Are there any relatives who might have information about this person? Once the member is located, he should be contacted by telephone if possible. Since the member paid consistently prior to his son's death, he may be under the mistaken notion that he is not required to pay the loan once the son is dead. Explain the member's obligations to repay the loan, and then get him to commit to resuming payments. Once you have reviewed both cases and their solutions, use any remaining time to answer student questions.

### **COMMUNICATIONS SKILLS (20 minutes)**

- Facilitate 20 minute activity in which you have Participants identify the communication skills required for dealing with delinquent members.
- To manage the time, allow about 10 minutes for the Participants to come up with their ideas, and 10 minutes to discuss them.
- Introduce the activity with the following.
- It takes special communication skills to deal with delinquent members.

### **Case Study**

- On the one hand, they are members, so you want to treat them with the respect and dignity they deserve.
  - On the other hand, they are delinquent, so you want to be clear and firm about their obligation.
  - Let's form into small groups and identify the communications skills necessary for handling delinquent members.
- Process
- Break the large group into smaller groups of 4-6 people each.
  - Allow the groups 10 minutes to identify as many communications skills as they can.
  - When the discussion time is up, bring the small groups back together into a large group.
  - Allow 10 minutes for them to share their answers, and then add those that you feel are important.
  - The Participants will come up with many responses. Following are some of the most important.

**Ability to inspire trust**—the member will be willing to discuss his situation only if he trusts the loan professional.

**Listening skills**—the loan professional must be willing to give his undivided attention to the member. Otherwise, he will not be able to understand the member's situation.

**Ability to draw the member out**—the loan professional must know which questions to ask to get the member to talk.

**Ability to empathize**—the loan professional must be able to understand the member's situation in order to work with it effectively.

**“Non-judgmental”**—the loan professional can't look down upon the member or act in disdain over his difficult financial status.

**Willing to work with the member's problems**—the loan professional needs to handle the member's financial problems as though they were his own.

**Firm, but tactful**—the loan professional needs to be very clear about the member's obligation, but also needs to communicate it without sounding harsh.

**Facilitative**—the loan professional needs to be able to lead the member through the problem-solving process.

**Positive thinker**—the loan professional needs to assume that the member wants to pay the loan and clean up his financial record.

### **CASE STUDY—ANALYZING A DELINQUENCY REPORT (30 minutes)**

To facilitate the case study, you can either copy the case study page distribute it to Participants, or read the data from the case to Participants. You can also write the data on the chart. Just be certain that it is visible to all Participants.

To manage your time, allow about 15 minutes for Participants to analyze the data, and 15 minutes to discuss the Participants' conclusions.

- For best results, you may wish to assign Participants to work in groups or teams. By working together, they can generate conclusions from each other.
- Read (or show) the case study data to the Participants.
- Tell them that their job is to study the data, and then write down their conclusions.
- To get the Participants started, you may want to generate one or two conclusions as a large group.
- Then, once Participants appear to understand the project, encourage them to work in their groups.

When time is up, call the small groups back together and lead a discussion.

Ask Participants to share the conclusions they formed.

Add any that you feel are important.

The Participants will come up with many conclusions. Following is a list of some of them.

The credit union's delinquency ratio is acceptable, but not ideal.

With one exception, all delinquency ratios spiked from January to February. It might be worthwhile to analyze if there was an unusual problem or occurrence that month.

Working Capital loans are consistently higher than the credit union's average. Perhaps it would be worthwhile to examine the policies and procedures used for granting Working Capital loans.

First-time loans have a good ratio. Perhaps it would pay to analyze the policies and procedures used for granting these loans, and then consider adopting them to Working Capital loans.

Once all Participants have had a chance to share there conclusions, use any remaining time to answer their questions.

**CASE STUDY—ANALYZING A DELINQUENCY REPORT** Study the following delinquency report and write down your conclusions.

#### **First Quarter Delinquency Ratios**

<b>Type of Loan</b>	<b>January</b>	<b>February</b>	<b>March</b>
Microfinance Working Capital	9.7%	9.9%	10.3%
Agriculture Credit loans	6.1%	8.0%	12.3%
Collateral loans	4.6%	4.9%	5.0%
First-time loans	8.3%	8.6%	7.9%
<b>Total credit union Loans</b>	<b>7.7%</b>	<b>8.1%</b>	<b>8.1%</b>

Conclusions



