

Friday, April 10, 2009

Eastern Financial ordered to cease ‘unsafe and unsound’ practices

South Florida Business Journal - by [Brian Bandell](#)

State regulators have given Eastern Financial Florida Credit Union a long and arduous to-do list. At the top: Hire effective leadership.

Even though it's South Florida's largest credit union, Eastern Financial has not had a permanent CEO since Stephen McGill resigned in February 2008. It will need strong leadership to address the issues raised in a March 19 order from the Florida Office of Financial Regulation (OFR) that listed 15 "unsafe and unsound" practices the credit union must cease and desist.

On a 10-point scale of severity of regulatory orders, this is an eight or nine, Miami-based banking analyst and economist Kenneth H. Thomas said. It addresses nearly every area of concern for banking operations, including capital, loan quality, management and compliance with regulations.

"Considering the present condition of this credit union and the contents of this cease and desist order, my only question is: Why wasn't this cease and desist issued last year?" Thomas said. "I guess better late than never?"

Eastern Financial ended 2008 with \$1.69 billion in assets. It lost \$40.2 million last year, allowing its net worth-to-total asset ratio to fall to 6.5 percent. Regulators require a 7 percent ratio for a well-capitalized credit union.

The order required the credit union to submit a plan to restore its net worth to well-capitalized levels. How that will happen is unclear because credit unions are nonprofits and must raise money through profitable operations rather than attracting investors.

Facing further losses

Unfortunately, Eastern Financial likely faces further losses since it had \$67.1 million in delinquent loans, representing 5.1 percent of its total loans, plus \$32 million in foreclosed real estate on Dec. 31. It had set aside reserves of about \$28.2 million to deal with them.

Eastern Financial is the only Florida credit union to get zero stars from Coral Gables-based Bauer Financial, which analyzes banks and credit unions. Most Florida credit unions get four- and five-star ratings from Bauer.

On March 20, the National Credit Union Administration placed two of the nation's largest corporate credit unions into receivership. The federal agency is also seeking \$30 billion in emergency borrowing authority, five times its usual base level.

The NCUA is the equivalent of the Federal Deposit Insurance Corp. for credit unions, and deposits are insured to \$250,000.

The OFR ordered Eastern Financial to evaluate all its executive positions for weaknesses and hire additional executives, including a permanent CEO. The OFR has the right to review – and potentially reject – executive hires.

“We are addressing the concerns quickly and fixing them so we can come out of this recession sooner than other financial institutions,” Eastern Financial said in a statement.

Eastern Financial needs a talented and motivated CEO to address its challenges, but that person won't be able to do it alone, said **Dennis Nason**, CEO of Coral Gables-based **Nason and Nason**, an executive recruitment and staffing firm for the financial industry. During the several months it takes to hire this leader, the credit union should bring in teams of temporary employees to tackle all the issues regulators raised, he said.

Unfortunately, hiring these people and starting programs to comply with the order would cost Eastern Financial money.

“Its very survival will rest in how they handle things in the next 180 days,” he said.

Re-evaluating policies

The OFR ordered Eastern Financial to designate an executive officer not involved in day-to-day lending to re-evaluate the credit union's policies for reserving for loan losses.

Most of the delinquent loans plaguing Eastern Financial came from member business loans, which include construction and commercial real estate loans. On Dec. 31, it reported that about a quarter of its \$201.5 million in member business loans were delinquent.

While Eastern Financial could not legally foreclose on a current loan to comply with this order, it could reduce the balance of large loans by selling off portions of them to other lenders, Nason said. However, it would likely take a loss on such deals.

“This is a credit union that is on a very short regulatory leash, where every major decision may be second-guessed by the regulators,” Thomas said. “So, borrowers can likely expect the credit union to take the absolutely most conservative actions across the board.”