American Bankers Association
Building Success. Together.

Brittany Dengler
Senior Research Manager
P 202-663-5356
bdengler@aba.com

August 28, 2015

Gerard S. Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314-3428

Re: National Credit Union Administration; Member Business Loans; Commercial Lending; 12 C.F.R. Part 701, 723, and 741; 80 Federal Register 37898, July 1, 2015

Dear Mr. Poliquin:

The National Credit Union Administration (NCUA) has requested comments on a proposal which would amend its member business lending rule governing federally insured credit unions (credit unions). The proposed rule would replace the current member business lending rule's requirements with a broad principles-based regulatory approach.

ABA's Position
While the American Bankers Association[1] (ABA) is supportive of efforts to reduce regulatory burdens, ABA is strongly opposed to this proposal and believes the proposed amendments are contrary to congressional intent to limit business lending activities by the credit union industry. In addition, not only does the proposed rule encourage credit unions to divert credit union member resources to finance commercial businesses, it also relaxes safety and soundness regulations associated with these types of loans. The amendments set forth in this proposal will lead to safety and soundness concerns as business lending regulations become increasingly lax and increased commercial lending becomes more appealing to the credit union industry.

Overstepping Regulatory Reach by Expanding Business Lending Loopholes
In 1998, Congress made it clear that credit unions should be focused on consumer lending, not commercial lending. Congress instituted restrictions on business lending deliberately to ensure that credit unions maintain a consumer focus. The report of the Senate Committee on Banking, Housing & Urban Affairs clearly supports this position:

> "…the Committee imposed substantial new restrictions on business lending by insured credit unions. Those restrictions are intended to ensure that credit unions continue to fulfill their specified mission of meeting the credit and savings needs of consumers, especially persons of modest means, through an emphasis on consumer rather than business loans. The Committee action will prevent significant amounts of credit union resources from being allocated in the future to

[1] The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's $15 trillion banking industry and its 2 million employees. Learn more at aba.com.

> large commercial loans that may present additional safety and soundness concerns for credit unions and potentially increase the risk of taxpayer losses through the National Credit Union Share Insurance Fund…"[2]

However, the proposed rule encourages credit unions to divert member resources to financing large commercial enterprises by relaxing the regulatory requirements to make these loans. By proposing this rule, NCUA has blatantly disregarded congressional intent.

For years, there has been little dispute over the fact that the statutory member business loan (MBL) cap is 12.25 percent of assets—mandated by Congress through the Federal Credit Union Act (FCU Act). Indeed, NCUA's current Chairman testified twice in 2011 that 12.25 percent of assets is the member business loan cap. However, some NCUA Board members have claimed that this proposed rule and some creative statutory interpretation would allow some credit unions to increase their MBL caps. ABA believes that this interpretation of statue is incorrect and would call on NCUA to clarify that the MBL cap will remain at 12.25 percent for all credit unions as mandated by the FCU Act.

Circumventing Congressionally Mandated Aggregate Member Business Loan Limit
In the proposed rule, NCUA reiterated that nonmember business loans and participating interest (NMBLs) are excluded from the aggregate MBL cap. By excluding NMBLs from the aggregate MBL cap, NCUA is directly circumventing the congressionally mandated MBL cap. If Congress intended to allow the NCUA Board to exclude forms of business loans from the MBL cap, it would have articulated this is Section 107A of the FCU Act—but it did not. NCUA is overstepping its authorities in excluding NMBLs from the MBL cap.

Furthermore, these loans are excluded from both the seller's and purchaser's aggregate MBL cap—this means that these loans are *not included in any business loan-limit calculation*. This could make the statutory MBL cap meaningless by allowing creative credit unions to hold a significantly higher portion of business loans than is permitted under the statutory cap, by selling and buying participations. In theory, NCUA prohibits credit unions from using this 'tool' as a way to circumvent the congressionally mandated MBL cap. However, NCUA has **<u>not</u>** articulated how this would be enforced or monitored nor has NCUA demonstrated an ability to do so. Excluding these business loans from any business loan-limit calculation will create an extremely dangerous situation.

ABA would appreciate clarification from NCUA on how it would enforce and monitor credit unions to ensure these transactions are not in fact being used to circumvent the MBL cap.

In the extreme, all business loans could be excluded from the limitation if they were merely bought and sold among credit unions. While the extreme is perhaps unlikely, the exclusion of these loans constitutes an underestimate of the business loan exposure and results in a false impression that the concentration limits imposed by Congress have been met. In addition,

---

[2] Senate Banking Committee Report (105-193).

improperly reflecting the total business loan exposure is counter to proper risk-management oversight expected of a federal financial institution regulator.

The Board should rescind this provision of the proposed rule. Furthermore, NCUA should clarify that all NMBLs should be included in any business loan-limit calculation, other than those enumerated in the FCU Act.

Poses Serious Safety and Soundness Concerns

At the same time the NCUA's proposal circumvents congressionally-mandated limits on member business loans, it is also relaxing its safety and soundness standards that apply to these loans—posing serious safety and soundness concerns.

For example, in 2010, NCUA issued a final rule requiring all credit unions to obtain personal guarantees from commercial borrowers. The Board "believed obtaining the principals' personal guarantee is a prudent underwriting practice that greatly enhances the likelihood of loan repayment and should be required of all credit unions." NCUA also stated that "a credit union that fails to do so subjects itself to increased risk…"[3] However, the current proposal removes this requirement which NCUA felt was necessary to protect consumers, credit unions and the National Credit Union Share Insurance Fund only five years earlier.

In addition, NCUA is proposing to remove already lenient regulatory policies, such as, loan-to-value limits, aggregate limits on construction and development lending and minimum borrower equity on construction and development lending. Such a relaxing of regulatory standards will not only encourage credit unions to divert member funds from consumer lending to commercial lending, but also will create serious safety and soundness concerns as the credit union industry, with limited experience and a lack of underwriting expertise in business loans, ramps up business lending activity. ABA has serious reservations about the dilution of the regulatory standards for credit union business lending.

NCUA has not established that it is prepared to supervise institutions with expanding business loan portfolios, and the credit union industry has proven ill-equipped to make such loans. At least five credit unions since 2010 have failed at the hands of poorly run business loan programs, accounting for a quarter of all losses to the insurance fund during that period. In 2010, member business loans were the primary or secondary contributing factor for the supervisory concern for nearly half of the credit unions with CAMEL ratings of 3, 4 or 5 that made business loans. The level of delinquent member business loans dramatically rose from 0.53 percent in 2006 to 4.29 percent in 2010; compared to a total loan delinquency of 1.74 percent, this is a clear indication that credit unions, and NCUA itself, were ill-prepared for the additional responsibilities and risks associated with commercial lending. Losses could quickly multiply under this proposed rule.

Furthermore, relaxing the regulatory standards is contrary to NCUA's charge of protecting the industry's insurance fund, and effectively places the taxpayer at risk. NCUA is willfully ignoring

[3] 12 CFR Parts 701, 723 and 742.

lessons from their history which may lead to serious consequences for not only the credit union industry, but all involved in business lending—including business owners.

Oppose Broadening Current Lending History Exceptions
As a final note, ABA would like to express its opposition to any attempts by NCUA to broaden its current interpretation of the lending history exception. When Congress enacted the statutory MBL cap it provided two exemptions. The first to credit unions chartered for the purpose of making commercial loans and the second to credit unions that had a history of primarily making business loans. The proposal notes that NCUA will continue to apply the "history of primarily making member business loans" exemption by referencing to the data of Credit Union Membership Access Act's enactment. The NCUA's current interpretation of the lending history exception reflects congressional intent and is therefore supported by ABA. ABA is extremely opposed to any broadening of this interpretation as an attempt to extend the exemption to a wider array of credit unions.

Conclusion
In conclusion, ABA opposes NCUA's proposal to amend its member business lending rule governing federally insured credit unions is against congressional intent to limit credit union business lending and could adversely affect the safety and soundness of a credit union. ABA believes NCUA should not proceed with this proposal.

ABA appreciated the opportunity to share its views and would be happy to discuss any of them further at your convenience. If you have any questions, please contact Brittany Dengler at (202)663-5356 (e-mail: bdengler@aba.com).

Sincerely,

Brittany Dengler
Senior Research Manager
Office of the Chief Economist