From: John McKenzie
To: _Regulatory Comments
Subject: Indiana Credit Union League Comments on NCUA Proposed Rulemaking for Part 723 - Member Business Lending
Date: Sunday, August 23, 2015 6:07:51 PM

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

Re: Proposed Rulemaking for Part 723 - Member Business Lending

Dear Mr. Poliquin:

The Indiana Credit Union League (ICUL) appreciates the opportunity to submit comments on the National Credit Union Administration's Proposed Rulemaking for Part 723- Member Business Lending (MBL). The ICUL member credit unions represent 97% of assets and members of Indiana's credit unions, with those memberships totaling more than two million consumers.

We appreciate the NCUA Board thoroughly reviewing the MBL rule and modernizing the rule in a way that provides greater flexibility to credit unions making these loans, streamlining the process by eliminating the requirement for waiver requests, and providing some needed regulatory relief against the arbitrary cap that is in place.

We support NCUA's move to a principles-based rule and away from a prescriptive, inflexible rule. It is important that credit unions have the flexibility to manage their commercial lending programs with the ability to adjust as necessary to meet the needs of the membership. We support eliminating those restrictive requirements from the rule that are not specifically required by the Federal Credit Union Act (FCUA). We would encourage NCUA to utilize this approach with other regulations.

We agree with the addition of the definition of commercial loans as well as the distinction between what is a commercial loan and what is a member business loan and subject to being included in the MBL cap calculation. This clarification that better aligns the MBL regulations with the FCUA is an important change that positions credit unions to develop commercial loan programs that are structured to meet the membership needs while recognizing the importance of sound policies and procedures to manage the commercial loan portfolio.

We support eliminating the loan-to-value ratio limitation, secured loans-to-one borrower limitations, and personal guarantees, and allowing a credit union to address these in its commercial loan policy. Eliminating these from the rule does not mean that credit unions will not establish their own criteria for these various ratios/limits, or no longer require personal guarantees. Credit unions will continue to apply sound lending criteria, and establish appropriate safeguards. It is important that NCUA is allowing the credit union board and management to determine what the appropriate limits and borrower requirements are, and when to waive certain requirements to facilitate making high quality commercial loans. Credit union staff have provided many examples where a good, quality member business loan was not made due to delays resulting from the waiver process.

NCUA is maintaining in the regulation a limit on loans to one member or group of members at 15% of net worth. We recognize that the proposal allows a credit union to go up to an additional 10% of net worth if the additional amount is fully secured by readily marketable collateral. While we are encouraged that NCUA has eliminated the necessity for requesting waivers in many areas, we ask that NCUA consider allowing for waiver requests for this one limit. While 15% of net worth may sound like a lot, for small- and medium sized credit unions this could be reached relatively easily. We have seen in Indiana, particularly with credit unions involved in agricultural lending, that this limit has created issues, forcing credit unions to participate out high quality, high yielding loans. The ultimate impact is reduced earnings for the credit union initially making the loan, or the loan going to a larger lender with greater flexibility.

We concur with the proposed treatment of 1- to 4-family (owner occupied or non-owner occupied) residential loans as not being commercial loans. We also agree with not counting 1- to 4-family owner occupied toward the MBL cap. We understand the specific requirement of the FCUA that 1- to 4-family non-owner occupied residential loans be treated as MBLs for purposes of the MBL cap calculation. We continue to believe that additional statutory changes are needed, and would encourage NCUA to support legislation that would address some of the limiting MBL restrictions in the FCUA.

We support the proposal to exclude non-member loans purchased in whole or a participation interest of a non-member loan purchased from the MBL calculation. This does not mean that the credit unions do not need to do due diligence and follow the commercial loan regulations and loan participation regulations as they apply to these loans. Loan participations are an important tool for credit unions to manage the MBL concentration, liquidity, and overall risk. Participations also facilitate collaboration among credit unions, which is fundamental to the cooperative nature of credit unions. This proposal provides greater flexibility to credit unions utilizing this important risk management tool.

We agree with the proposal to eliminate the two-year experience requirement. The credit union's overall staff experience in managing the risk associated with commercial lending is what is important. The ability to utilize third party providers in this environment to meet the overall experience expectations remains important. We encourage NCUA to continue to look at the combination of the credit union staff and third-party provider's staff experience when evaluating this area. We also recognize the overall responsibility of the credit union's board and management to understand the types of loans that the credit union is making, regardless of whether staff or a third party is doing the underwriting and ongoing risk management of the loan portfolio. We support this being dealt with through the supervisory and examination process.

We agree with the proposal to eliminate the reference to 12.25% of assets and only referring to the MBL cap as "1.75 times the net worth ratio required to be well capitalized" as it is defined in the FCUA. This allows flexibility in the calculation should the net worth requirements to be well capitalized change. Many comments from the banking industry distort the impact that this will have. Analysis shows that for most credit unions, 7% of total assets exceeds 10% of risk assets (well capitalized in proposed risk-based capital rule) resulting in no increase in the cap. The overall impact for credit unions is estimated to be .1%, or an increase to 12.35% of assets, a negligible increase at best.

We support the proposal to exempt credit unions with assets less than $250 million and total commercial loans less than 15% of net worth that are not regularly originating and selling or participating out commercial loans from having to develop a full commercial loan policy and commercial lending organizational infrastructure. It remains important that these credit unions address the types of commercial loans authorized, the complexities of this type of lending, underwriting requirements, lending limits, staff ability to manage the risks associated with this type of lending, etc., in the general loan policies. As NCUA examines these credit unions, the same review of these loans will occur based on the supervisory guidance, and the credit unions should be able to demonstrate the ability to manage this lower amount, but having a similar risk profile, as if they had the full commercial loan policy in place.

In the proposal it is stated that "NCUA will incorporate expectations regarding risk management practices, such as LTV ratios and portfolio concentration limits, into supervisory guidance issued with any final rule adopted by the board." It is important the supervisory guidance developed maintain the flexibility intended with the proposed rule. Often examiners equate supervisory guidance as equivalent to regulation, and require more or impose restrictions not included in the regulation, but referenced in the supervisory guidance as "best practice," "limits that should be considered," etc. Care needs to be taken that the benefits from the revised rule are not muted or reduced by the supervisory guidance. We encourage NCUA to put the supervisory guidance, once developed, out for public review and comment. This will allow all parties to feel comfortable that the prescriptive limitations of the current regulations are not being simply moved to supervisory guidance, and the intended beneficial impact of the new regulations is made moot by the guidance.

The proposal is recommending an effective date of 18 months after the proposal is finalized. We would like to see NCUA allow credit unions that are prepared to follow the new requirements earlier than 18 months after the final rule be allowed to do so at their discretion. We believe that this will allow those credit unions to begin benefitting from the intended regulatory relief as soon as they are positioned to do so.

NCUA is estimating a one-time $1.9 million cost to the agency to implement the proposed rule. We believe that it is important that NCUA cover this one-time expense by reallocating existing resources, and not as an add-on to NCUA's budget.

The banking industry has been very active in submitting form letters that include a variety of erroneous claims related to the ability of credit unions to be involved in commercial lending. They continually reference the information NCUA provided in the commentary on the proposed rule referring to losses incurred by the share insurance fund resulting from five credit unions involved with MBL during the economic downturn. During the same time frame, the FDIC suffered much more significant losses that had a greater impact on their fund. Credit union experience with MBL delinquency and chargeoffs was no different than what banks experienced during the economic downturn. NCUA has stated in the write up accompanying the proposed regulation that "As the economy has recovered from the recession, the performance of credit unions' business lending has improved. The delinquency and chargeoff rates of business loans continue to decrease and revert to pre-recession levels. Delinquency and net charge-off rates in 2014 dropped to 85 bps and 28 bps respectively, from 406 bps and 81 bps in 2010." The St. Louis Federal Reserve Bank shows commercial bank delinquency rates on business loans increasing form 115 bps at the end of 2006 to 430 bps at the end of 2009, and commercial loan chargeoff rates increasing from 30 bps to 256 bps over this same timeframe. Similar to what credit unions have experienced, bank business loan delinquency and chargeoff rates have returned to pre-recession levels.

Additionally, banker comment letters reference that NCUA has not demonstrated an economic need for this proposed regulation. This proposed regulation is about providing regulatory relief. Small businesses have reached out to credit unions as a source of credit when the banks either reduced or were unwilling to provide credit to these same businesses during the economic downturn. This proposal allows the necessary flexibility to work with these businesses to more effectively meet their needs in today's economic environment.

Banker comments also refer to taking "member" out of "member business loan" by removing the requirement for a personal guarantee. Credit unions will continue to make loans to members. The personal guarantee is not what defines a member. The proposal would facilitate the ability of credit unions to make quality loans without unnecessary stipulations that would not be required of the member at other financial institutions. Personal guarantees do not go away completely, but would be addressed in the credit union's commercial loan policy.

Additional comments from the banking industry include other erroneous claims. As stated above, the elimination of the 12.25% of assets referenced in the existing regulation simply aligns the proposed regulation with the FCUA, and, in reality, has very little or no impact on increasing the cap for the vast majority of credit unions. The FCUA only specifies that the MBL cap is "1.75 times the net worth requirement to be well capitalized." Credit unions are tax exempt based on their member-owned cooperative structure, not based on the services they offer. The proposal allows the credit union to address loan-to-value caps, loans to a single borrower, and personal guarantee in the commercial loan policy. This again allows the credit union to manage its MBL program in a way that provides prudent protection along with the flexibility to meet the needs of its members without being burdened by arbitrary limits not specifically required by the FCUA.

Thank you for the opportunity to comment on the proposed member business lending regulations. We are encouraged that NCUA was willing to approach this revision in a way that provides regulatory relief to credit unions offering MBLs. We hope that through the issuance of supervisory guidance, NCUA does not undermine the regulatory relief intended in this proposed regulation. We continue to believe that the 1.75 times net worth required to be well capitalized MBL cap is an arbitrary and unnecessary statutory restriction on credit unions and would hope that NCUA would support legislation intended to rectify this.

We appreciate the desire of NCUA to provide regulatory relief and ask that this continue to be the focus of new and proposed regulatory changes. If you have any questions about our letter, please do not hesitate to give me a call at (317) 594-5320.

Sincerely,

John McKenzie

John McKenzie
President, Indiana Credit Union League