Open Board Meeting June 18, 2015

NCUA Chairman Debbie Matz
Statement on the Proposed Member Business Lending Rule

This principle-based rule is the right approach at the right time. After Congress placed new limits on member business lending in 1998, NCUA wrote a series of prescriptive rules to ensure sound underwriting, solid collateral and experienced management.

For many years, the prescriptive approach may have been appropriate as credit unions entering the business loan marketplace gained experience. Today, however, the vast majority of credit union business lenders have well-established, solid commercial lending infrastructure and sound risk management policies.

The results have been quite remarkable: Over the last 15 years, the credit union system's total business lending portfolio has grown more than 12 times larger, from $4 billion in 2000 to more than $51 billion today. Yet, delinquencies and charge-offs for commercial loans at credit unions overall indicate solid performance. The credit union system as a whole has grown its commercial lending portfolio in a safe and sound manner.

Now is an appropriate time to transition away from prescriptive regulatory limits toward general principles that will provide credit unions greater flexibility to serve business owners. This is important because member business lending produces three tangible benefits:

- It provides affordable small business loans (with an average balance of $217,000), which business owners may not be able to obtain from other institutions;
- It diversifies loan portfolios, improving credit unions' ability to withstand economic downturns; and
- It develops communities by creating jobs and expanding consumers' access to local goods and services.

Of course, commercial lending may not be appropriate for every credit union. It's a strategic decision for each board of directors to make. Once they decide to engage in member business lending, as long as they comply with the statutory cap, each credit union would have the freedom to prudently write their own business loan policy without prescriptive regulatory limits.

However, credit unions with small commercial loan portfolios would not even have to write a policy. Based on current volume, nearly 700 credit unions (about one in three commercial lenders) would be exempt from the policy requirement altogether. For example, credit unions that may just make an occasional commercial loan for a truck or a pizza oven would be able to serve those small business owners without additional paperwork.

As I've traveled the country to hold Listening Sessions and speak at credit union conferences, I've heard directly from credit union officials about specific operational challenges they face with NCUA's current MBL rule. This proposal completely rewrites the current rule to address those challenges and remove unnecessary burdens. For example:

- **Personal Guarantees —** I've heard loud and clear that requiring a personal guarantee on every business loan can lose business. Even though our Regional Offices approve most requests to waive personal guarantees, some members don't wait for waiver approvals; they take their business to other lenders. Under our proposed rule, the credit union could make the decision to waive a member from a personal guarantee.

- **Loan-To-Value Limits —** I've also heard that prescriptive LTV limits are sometimes an obstacle to serving business owners. Like personal guarantees, our Regional Offices do approve waivers of LTV limits wherever reasonable. However, we recognize that the primary focus in commercial lending needs to be on the borrower's ability to repay based on the business' operations, not collateral. That's why we're proposing to remove LTV limits and remove the waiver process altogether.

- **Construction & Development Loans —** I've visited the Dakotas and other states where credit unions are playing key roles in financing emerging businesses. Credit union officials provided very thoughtful feedback, which compelled us to reconsider our policy of placing lower limits on construction and development loans. That's why we're proposing to lift all unnecessary limits on these types of loans.

- **Loan Participations —** Credit union officials also urged us to remove any unnecessary barriers on loan participations, which help credit unions pool and diversify risks. That's why this proposed rule clarifies that participation interests in loans to non-members do not count against the statutory member business lending cap. Of course, we recognize that commercial loans still pose unique risks and require specialized oversight. When this rule becomes final, we plan to update guidance for credit unions and supervise effectively for sound commercial lending practices.

Changing the way we do business will require retraining our examiners. Retraining will take some time and resources to implement; but it will be well worth the effort. This modernized and flexible rule, implemented by well-trained examiners, would allow credit unions to safely and soundly serve more of America's small business owners.

This new rule would also apply to most state-chartered credit unions that make commercial loans. For the seven states with their own member business lending rules (which were previously approved by NCUA), the proposal presents options for comment.

We recognize that some state-chartered credit unions might prefer this new NCUA rule, while some state regulators might prefer their own state rule. As a result, we're seeking comments on whether the seven existing state rules should be grandfathered, and whether any state should continue to have the opportunity to apply for NCUA approval of a state commercial lending rule in the future. We look forward to the comments on this issue, and on all aspects of our proposal.

Clearly, this proposal will provide real regulatory relief, which credit unions have requested, and empower credit unions to responsibly serve the needs of more members with small businesses. The bottom line is: Credit unions know their members better than we do, and our modernized business lending rule will reflect that fact.