UTAH BANKERS ASSOCIATION

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August 18, 2015

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

Re: Comments on Advanced Notice of Proposed Rulemaking for Part 723

Dear Mr. Poliquin,

The Utah Bankers Association (UBA) appreciates the opportunity to submit the following comments on the proposed amendments to Part 723 governing member business loans. UBA is the primary trade association representing every kind of banking institution in Utah. We hope you find our comments helpful.

UBA's members are keenly interested in business lending by credit unions. UBA has consistently supported credit unions organized to provide affordable personal loans to members of discrete, well defined groups. However, it is important to note that Congress granted certain advantages to credit unions to help them fulfill this mission including, most importantly, exemption from taxation. Credit unions were never intended to use these advantages to directly and unfairly compete with banks in the mainstream financial markets.

Nevertheless, a few credit unions in our state have combined to form some of the largest depository institutions in Utah and have aggressively expanded their fields of membership to include the majority of residents in the state. These large credit unions operate like banks and directly compete with banks while offering a full array of consumer financial products and services. As a result, banks that are taxed find it increasingly difficult to offer competitively priced consumer loans and accounts. Many banks have largely abandoned those markets and now focus more on commercial loans and services.

There is no question that Congress did not intend to give credit unions a competitive advantage when it exempted credit unions from income tax. Instead, it intended to give credit unions the ability to better serve people who were underserved. Since that was their intended mission, credit unions were also exempted from the community reinvestment laws. In that regard, perhaps the most perverse regulatory feature of the current financial services markets is the fact that the large bank-like credit unions have no obligation to serve the underserved parts of the communities within their geographically defined fields of membership while the tax paying banks competing in those same areas do have that obligation and now are the primary providers of financial products and services to the underserved in those communities.

Another feature of the development of large credit unions into direct competitors with banks is their increasing encroachment into the commercial loan markets. This is where banks can still compete on level terms and provide vital products and services to the businesses in their communities. For that reason, our members have deep concerns about any expansion of credit unions' ability to expand in these markets, and our members sincerely appreciate NCUA giving its

close attention to the proposed amendments to ensure that they do not lead to more unequal and unfair competition with taxable banks.

With this background, we will now address the specific changes proposed for Part 723.

To begin, we found the information regarding the growth in commercial lending concerning to the extent that it represents increasing direct competition with banks. It shows the extent to which credit unions will encroach further into commercial lending markets if allowed to do so. This growth should not be viewed as a proper reason to relax commercial lending rules. If anything, it shows the need to tighten restrictions.

As NCUA notes in its narrative explaining the proposed rule, it will substantially change the NCUA's overall approach to regulating commercial lending and will ". . . provide federally insured credit unions with greater flexibility and individual autonomy in . . . making commercial and business loans . . .". UBA urges NCUA to reconsider this goal and revise the proposed rule, or amend the existing rule, to ensure that it does not enable credit unions to engage in increased unfair competition with tax paying banks. Expansion of any credit union lending activity should be limited to underserved groups and should not enable a credit union to use its competitive advantage to enter markets already served by banks.

Proposed Section 723.2—Definitions. UBA supports the new language clarifying that a loan secured by a vehicle to carry fee paying passengers is a commercial loan. Banks have encountered problems with borrowers who use their personal vehicles to drive for Uber or other smart phone based ride services. Too often the vehicle lacks the insurance needed for a commercial activity and the collateral is unprotected from loss or damage incurred while engaged in ride share activities.

Proposed Section 732.3—Board of Directors and Management Responsibilities. UBA notes the absence in this section of any direction to boards and management to avoid engaging in unfair competition with other kinds of financial institutions and expanding into areas already adequately served by other financial institutions.

Section 723.5—Collateral and Security. The proposed rule would eliminate the requirement for a member to personally guarantee each business loan. UBA urges NCUA to retain that requirement. While that may not always be necessary for underwriting purposes, it is consistent with the principle that credit unions only make loans to members and a commercial loan is a loan to a member for business purposes.

The proposed rule would also eliminate specific collateral requirements and instead state that each business loan should be appropriately collateralized. The rule would note that collateral is not always required if repayment is reasonably likely unsecured. UBA urges NCUA to not make this change. The purpose for the change is to give credit unions added "flexibility" to make business loans, which should not be allowed without adequate controls to ensure that a credit union will not use the added flexibility to compete in markets already served by other financial institutions unable to compete on equal terms with the credit union.

Section 723.6—Construction and Development Loans. UBA does not oppose allowing individual credit union members to borrow for the purpose of constructing a home for themselves but we urge NCUA to reconsider whether a credit union should allow members to borrow for speculative real estate development. As NCUA notes in the narrative, this is a tricky area and despite proposed requirements for each credit union to have comprehensive policies and expertise before engaging in this kind of lending, many credit unions will simply not have the ability to competently evaluate the inherent risks inherent.

These risks are magnified if the new rule eliminates the requirement for personal guarantees. Developers routinely conduct development activities through legal structures that confine potential losses within a certain entity while protecting other assets in the event the development fails. Requiring personal guarantees would help ensure that only the lowest risk projects are funded.

Fraud is epidemic in this area and robust systems are needed to verify representations in an application. Requiring personal guarantees will help reduce the risk if NCUA decides to allow credit unions to make more of these loans.

UBA also urges NCUA to reconsider eliminating the requirement in the current rule, 723.3(b), requiring the borrower to have a minimum 25% equity interest in the project being developed. This is a prudent requirement that undoubtedly protected many credit unions from losses in the housing market downturn beginning in 2008. Other lenders, including some banks, followed the market as underwriting standards loosened to the point where some lenders required little or no "skin in the game". That intensified the speculative bubble that eventually disrupted the housing markets.

Section 723.8—Aggregate member business loan limit; exclusions and exceptions. The new proposed section would substantially change the current limits on aggregate business loans by exempting from the statutory limits commercial loans made to non-members. The current rule, 12 C.F.R. 723.16(b)(1) provides that all the total of all member and nonmember business loan balances ". . . must not exceed the lesser or 1.75 times the credit union's net worth or 12.25% of the credit unions net assets . . .". The new rule would change this by creating two categories of commercial loans, one being member business loans and the other not member business loans then applying the limits to only the member business loans.

UBA members strongly object to this change. It directly conflicts with Congress' intent to limit business loans in credit unions. Nonmember business loans are still business loans except they are effectively made to people and businesses that have no connection to the credit union or its field of membership. Congress enacted limits on business loans in statute in order to ensure that credit unions do not drift from their primary mission to serve the financial needs of their individual members. The proposed rule would allow a credit union to buy unlimited amounts of business loans provided they were not made to a member of the credit union.

We understand that the new rule provides that the exemption for nonmember commercial loans applies if the credit union ". . . is not, in conjunction with one or more other credit unions, trading member business loans to circumvent the aggregate limit." However, this qualification is inadequate to prevent a gross abuse of the exemption. For example, it would not prohibit a credit union from buying business loans from another credit union or any other business as long as they were not "trading" loans. A credit union could potentially hold nothing but nonmember business loans as long as it only acquired loans. It could then sell loans as long as the counterparties were not other credit unions.

It would even be possible for a group of individual members of a credit union to use federally insured deposits to engage in the sole business activity of buying originated loans from a commercial finance lender, which those members could even control.

Clearly this would be a substantial change in current business lending standards that goes way beyond the letter and spirit of the Federal Credit Union Act. We urge NCUA to stay with the current rule's simpler definition of business loan, which does not draw illogical and unjustified

distinctions between commercial and business loans, and subject all business loans to the statutory limits.

UBA hopes you find these comments helpful.

Sincerely,

Howard M. Headlee
President