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August 31, 2015

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

Re: Member Business Loans; Commercial Lending—Comments on Proposed
Rulemaking for Part 723

Dear Ladies and Gentlemen:

The Independent Community Bankers of America (ICBA)¹ appreciates the opportunity to provide comment on the National Credit Union Administration's (NCUA) proposed rule, *Member Business Loans; Commercial Lending—Proposed Rulemaking for Part 723* (Proposal). ICBA does not support any attempt by the NCUA to provide flexibility to federally insured credit unions that desire to increase their offering of commercial and business loans to members or their affiliates. The currently defined requirements that limit commercial lending by credit unions follow federal law and, by design, are intentionally put forth to minimize all commercial lending by credit unions. ICBA requests that NCUA formally adopt regulations that curtail commercial and member business lending by federally insured credit unions rather than expanding it to mitigate risk to the U.S. taxpayer in the next economic downturn and reflect the intent of Congress that federally insured credit unions should serve consumers exclusively with an emphasis on those consumers of modest means with a common bond. Any action to encourage the expansion of member business and commercial loans by the NCUA will result in jeopardizing the safety and soundness of all federally insured credit unions and place undue risk on the U.S. taxpayer.

¹ The Independent Community Bankers of America®, the nation's voice for more than 6,000 community banks of all sizes and charter types, is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education and high-quality products and services.

With 52,000 locations nationwide, community banks employ 700,000 Americans, hold \$3.6 trillion in assets, \$2.9 trillion in deposits, and \$2.4 trillion in loans to consumers, small businesses, and the agricultural community. For more information, visit ICBA's website at www.icba.org.

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The Proposal

The NCUA proposes to amend its current member business loan rule to give federally insured credit unions the ability to apply flexibility when providing commercial and business loans to members. The current requirements and limitations that govern policy around commercial and business loans would be replaced with abstract principles that seek to provide a framework for safe commercial lending. As part of this new framework, federally insured credit unions would be required to develop a formal commercial loan policy that establishes a risk management platform for commercial lending. However, credit unions with total assets of less than \$250 million and total commercial loans that are less than 15 percent of total net worth would be exempt from adopting a commercial loan policy entirely.

Under the proposal, a commercial loan would be defined as credit extended for a commercial, industrial, agricultural, or professional purpose with the following exceptions: (a) loans made by a corporate credit union; (b) loans made by a federally insured credit union to another federally insured credit union; (c) loans made by a federally insured credit union to a credit union service organization; (d) loans secured by a 1- to 4-family residential property regardless of whether the property is or is not the primary residence of the borrower; (e) loans secured by a vehicle manufactured for household or commercial use; (f) any loan fully secured by shares in the credit union making the extension of credit or deposits in other financial institutions; and (g) any loans to a borrower or an associated borrower with an aggregate balance of \$50,000 or less.

The proposal would require credit unions to create credit risk rating systems, where risk ratings would be assigned to commercial loans at inception of the loan and throughout the life of the loan. The risk rating would be based on both qualitative and quantitative factors that form a comprehensive analysis used to establish a level of risk. The board of directors for each credit union covered under the proposal would be charged with forming and approving a commercial loan policy. The commercial loan policy must address the types of loans permitted, the identified trade area, maximum loan amounts, qualifications required for the lending staff, the loan approval process, the underwriting standards, and the risk management processes. Prescriptive limitations on the types of collateral permitted to be pledged as part of the lending arrangement will be removed and replaced with a general principle on collateralization.

It is also possible that the statutory limit on member business loans could be interpreted so as to remove any reference to absolute percentages of allowable asset levels (i.e., 12.25% of total assets) and replaced with a requirement of 1.75 times the applicable net worth requirement for a credit union that is categorized as well-capitalized. Currently, the net worth requirement for a well-capitalized credit union is 7% but that could be raised if the proposed Basel III rules are adopted.

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ICBA's Comments

ICBA continues to be very concerned with NCUA's latest attempt to drive federally insured credit unions away from focusing on their narrowly specified mission of providing credit and savings opportunities to consumers, especially those consumers of modest means². Congress intentionally placed limits on the ability of federally insured credit unions to engage in anything but the most insignificant amounts of commercial lending to ensure that the National Credit Union Share Insurance Fund is protected from large losses that place direct burdens on the taxpayers of the United States and to keep credit unions focused on their mission. The proposal prominently identifies this very risk and confirms ICBA's fears with the following:

"...there have been instances where some credit unions have failed to adequately manage the risks of their business lending activities and this has led to their failure and, in some cases, losses to the National Credit Union Share Insurance Fund. Poorly managed business lending activities were a contributing factor in the failure of at least five credit unions since 2010."

Credit unions, by their established mission, are not equipped to provide a commercial lending solution for businesses of any scale or size due to their inability to properly invest the time and resources required to establish and maintain a robust commercial loan infrastructure. ICBA believes that the statutory cap on member business loans of 12.25% of total credit union assets is inflexible and is not subject to interpretation by regulatory officials.

However, it has come to our attention that various NCUA board members and staff personnel have indicated that this inflexible statutory cap can be interpreted more broadly, particularly if the Basel III like capital standards are implemented by the NCUA. By limiting member business loans to 12.25% of total credit union assets, Congress is able to ensure that any risks to the taxpayer are mitigated. **Any attempt to circumvent this limitation through new Basel III regulatory capital standards that results in a higher concentration of member business lending above this statutory cap defies Congressional intent.** Additionally, by engaging in any activity that could be viewed as promoting the further expansion of commercial lending by federally insured credit unions, the NCUA is openly disregarding the real risks that come with originating commercial loans with elevated risk characteristics that could jeopardize the share insurance backstop that protects depositors and task taxpayers with covering any additional losses.

Member business lending is a highly contentious issue which has been debated in Congress for more than a decade. The NCUA should not be permitted to end-run Congress with a proposal to significantly expand member business lending and other forms of credit union commercial lending and discard or weaken critical prudential safeguards.

² See the Senate report on Credit Union Membership Access Act, Committee on Banking, Housing, and Urban Affairs, May 21, 1998

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Of particular concern to ICBA is the proposed replacement of definitive requirements and limits on the collateral and security interests for commercial loans with a general principle that commercial loans must be appropriately collateralized. Using an abstract framework that requires sound judgment to determine appropriate collateral requirements in place of tangible limits that promote transparency among peer institutions is counterproductive to protecting the share insurance fund. Without tried and true measures for defining the minimum collateral amounts and types needed to properly protect the institution against future loss, the credit union is free to develop any commercial loan policy that minimizes the safety and soundness principles that should be governing the origination of commercial loans and maximizes the amount of risk that can be tolerated by prudential regulators. Such a policy places new risks on a credit union's credit risk management team to appropriately create, modify, and extrapolate collateral requirements with uncertain results, especially when the credit union has limited ability to handle the incremental overhead costs required.

The current cap on member business loans already contains a number of exceptions that undermine its purpose and integrity. For example, whole loans and loan participations purchased from other credit unions do not count toward the cap. **The NCUA proposal would greatly expand this loophole by removing the requirement that credit unions seek a waiver for such lending. This would allow large credit unions to engage in hundreds of millions and possibly billions of dollars of business loans outside of the cap.** ICBA notes that the NCUA has not included an economic analysis that shows a credible need for commercial lending by credit unions to their members. Before any proposal for commercial lending is introduced, the NCUA should provide supporting evidence that credit union members would benefit above and beyond the risks that are facing the insurance fund and the U.S. taxpayer and that the commercial banking system is not currently meeting the needs of commercial lenders.

Additionally, ICBA notes that the proposed rule removes the explicit requirement contained in the current rule that, in the case of commercial loans, credit unions obtain a personal guarantee from the principal(s) of the borrower. If credit unions are chartered to serve their members with a limited membership base, ICBA questions why those members would no longer be required to personally guarantee their own lending obligations. **Like the proposed elimination of collateral and security requirements, this is another example of the NCUA weakening loan standards so that credit unions can expand their commercial lending activities. ICBA requests that NCUA retain its current personal guarantee requirement for the borrower, as well as all currently existing collateral and security requirements for member business loans.**

The NCUA should answer the question why, given its frank lack of confidence in credit union business lending, it proposes to weaken critical prudential safeguards. Reckless business lending has already jeopardized the credit union system. Credit unions lack the experience and the expertise to safely conduct business lending, and the NCUA lacks experience in supervising business lending.

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Community banks that engage in commercial lending operate under a very robust commercial lending policy that is a tried and true framework for providing much needed credit to small businesses in the communities they serve and is subject to constant federal regulator and field level examiner scrutiny as economies change over time. Community banks operate in the commercial lending space by utilizing robust underwriting practices that are well adept at establishing a borrower's ability to repay a loan, the viability of any collateral pledged, and the track record of the borrower both as a customer of the institution and a small business owner. Community banks generally limit their commercial lending opportunities to those where the bank's loan management personnel have an intimate knowledge of the transaction before it is finalized and not before a thorough examination of the borrower's financial picture, the collateral securing the loan, and the borrower's ability to repay the loan is completed. When loans become troubled or impaired in any manner, the local community banker is the person most skilled in providing workout assistance to the borrower to ensure that the most favorable outcome possible is realized both for the debtor and the institution.

Contrast this infrastructure with a federally insured credit union, whose mission is to serve consumers with a common bond. Because credit unions are by statute limited to serving a specific set of consumers, providing commercial lending solutions for those consumers is not practical when one considers the amount of resources that are needed to ensure the safety and soundness of the activity. To provide a commercial solution without first building out the framework needed to perform quality underwriting and management, the credit union is placing its capital at risk in such a manner that fails to meet the needs of its member base.

The proposal also calls into question the tax exemptions enjoyed by credit unions because they are designed to accommodate the lending and deposit needs of consumers of modest means and of a common bond. The NCUA is concluding with this proposal that federally insured credit unions should no longer follow their narrowly-defined missions and become taxpaying community banks. It is impossible to reconcile the desire to formally expand commercial lending offerings by credit unions with their assertion that they should remain tax-exempt and not be treated like taxpaying banks.

ICBA appreciates the opportunity to comment on this proposal. If you have any questions or would like additional information, please do not hesitate to contact me at james.kendrick@icba.org or (202) 659-8111.

Sincerely,

/s/

James Kendrick
Vice President, Accounting & Capital Policy

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