CREDIT UNION ASSOCIATION OF THE DAKOTAS

August 28, 2015

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

RE: RIN 3133–AE37; Comments on Proposed Rulemaking for Part 723

Dear Mr. Poliquin,

The Credit Union Association of the Dakotas (CUAD) appreciates the opportunity to provide comment to the National Credit Union Administration (NCUA) with regard to the proposed amendments to Member Business Loans (MBL) under Part 723. To provide a brief background, the Credit Union Association of the Dakotas represents sixty-nine state and federally chartered credit unions in the states of North Dakota and South Dakota, whose assets total over $5.9 billion and who have more than 450,000 members.

CUAD fully supports the NCUA's efforts to provide federally insured credit unions with "greater flexibility and individual autonomy in safely and soundly making commercial and business loans to meet the needs of their membership." *80 FR 37900, July 1, 2015*. We believe this relief is long overdue and we appreciate the NCUA's steps forward to reduce the regulatory burden so our credit unions can better serve the communities in which they operate. CUAD makes the following recommendations regarding the NCUA's proposed rule and in some instances seeks clarification as discussed below.

The NCUA discusses that, "Oversight will focus on the effectiveness of the risk management process and the aggregate risk profile of the credit union's loan portfolio, as opposed to compliance with prescriptive measures. Responsible risk management and comprehensive due diligence remain crucial to safe and sound commercial lending, and it is expected that credit unions subscribe to these overarching principles in administering, underwriting, and servicing commercial loans." CUAD implores the NCUA to ensure that any future guidance that it issues on this topic preserves the flexibility that the NCUA is striving for in this proposed rule. Guidance and training for examiners needs to avoid reviewing a particular credit union's MBL portfolio in a one-size-fits all approach.

CUAD requests that any official guidance issued by the NCUA be shared with the credit union industry in advance. The NCUA should allow feedback and comments on any guidance that will surely be issued to explain the final rule. CUAD acknowledges that the NCUA is not required by law to issue guidance for public comment, but CUAD anticipates that the level of "guidance" that will accompany this final rule will be extensive. If nothing more than to have an opportunity to seek clarification should differing interpretations arise, having as much as confusion as possible ironed out before the effective date and subsequent examinations would be the most effective and efficient use of time and resources for both the NCUA and credit unions.

With regard for training, the NCUA should require that state examiners receive the same training as NCUA examiners do to guarantee that there will be consistency when a credit union's MBL program is reviewed.

The NCUA proposes that a final rule revising MBL and commercial lending under Part 723 will be delayed for 18 months. *80 FR 37911-37912*. CUAD requests that credit unions be allowed to operate under the final rule prior to 18 months provided the credit union has the appropriate policies, systems and personnel in place to comply with the final rule. Credit unions have been waiting a very long time for regulatory relief from the arbitrary caps imposed in the existing MBL regulations. If a credit union is able to meet the regulatory requirements of the final rule earlier than 18 months they should be afforded the flexibility proposed under this rule.

The NCUA proposes to exempt credit unions under a certain threshold and with total commercial loans of less than 15 percent of net worth that are not regularly originating and selling or participating out commercial loans from certain sections of the proposed rule. Specifically, proposed section 723.1(b) would provide that "this part applies to federally insured natural person credit unions, except that credit unions with both assets less than $250 million and total commercial loans less than 15 percent of net worth that are not regularly originating and selling or participating out commercial loans are not subject to § 723.3 and § 723.4 of this part." *80 FR 37914.*

CUAD supports the exemption of credit unions with total commercial loans less than 15 percent of net worth from the regulatory requirements to develop a full commercial loan program. However, CUAD is concerned regarding the possible interpretations of "regularly originating and selling or participating out commercial loans" and requests that NCUA remove this aspect of the exemption or, alternatively, provide further guidance as to what level of activity equates to "regularly" as used in this proposed exemption. The NCUA notes, that it, "is concerned that extending this exemption to credit unions over $250 million in assets could incentivize some credit unions, regardless of their capacity and member business loan needs, to unduly restrict the volume of business lending—a vital source of working capital and job creation—to avoid higher prudential standards." *80 FR 37901*. CUAD does not share the NCUA's concerns and does not believe extending the exemption to credit unions over $250 million will cause credit unions to restrict their volume of business lending. CUAD recommends that the exemption from § 723.3 and § 723.4 be

simplified and extend to all credit unions with total commercial loans less than 15 percent of net worth, thereby removing the proposed asset threshold and the proposed "regularly originating and selling or participating out commercial loans" language from the exemption.

As discussed by the NCUA in its summary of the proposal, "the proposed rule distinguishes between the safety and soundness objectives generally applicable to all loans for commercial, industrial, agricultural, and professional purposes and the statutory limitations affecting MBLs." *80 FR 37900*. To achieve its objectives the NCUA has proposed several new definitions including, "commercial loan." As proposed, "commercial loan" would mean, "any loan, line of credit, or letter of credit (including any unfunded commitments), and any interest a credit union obtains in such loans made by another lender, to individuals, sole proprietorships, partnerships, corporations, or other business enterprises for commercial, industrial, agricultural, or professional purposes, but not for investment or personal expenditure purposes." *80 FR 37915*. "Commercial loans" would be subject to the safety and soundness requirements in the proposed sections 723.3 through 723.7, however, not all "commercial loans" are MBLs that are subject to the statutory aggregated limits.

Excluded from the proposed definition of "commercial loan" are: "loans made by a corporate credit union; loans made by a federally insured credit union to another federally insured credit union; loans made by a federally insured credit union to a credit union service organization; loans secured by a 1- to 4- family residential property (whether or not it is the borrower's primary residence); any loan(s) to a borrower or an associated borrower, the aggregate balance of which is equal to less than $50,000; any loan fully secured by shares in the credit union making the extension of credit or deposits in other financial institutions; and loans secured by a vehicle manufactured for household use." *80 FR 37915.* CUAD fully supports the proposed exclusions from the definition of "commercial loan." However, CUAD urges the NCUA to exclude more types of loans that present very low or no risk of loss to the credit union. CUAD requests that the NCUA also exclude loans fully guaranteed by a federal or state agency from the commercial loan definition due to their zero risk they do not present any safety and soundness concerns.

With regard to the exclusion for loans secured by a vehicle manufactured for household use, the NCUA notes in its discussion that loans for the purchase of vehicles to carry fare-paying passengers are commercial loans. The proposed definition for "loans secured by a vehicle manufactured for household use" provides, "a loan that, at origination, is secured wholly or substantially by a lien on a new and used passenger car and other vehicle such as a minivan, sport-utility vehicle, pickup truck, and similar light truck or heavy duty truck generally manufactured for personal, family, or household use and not used as a fleet vehicle *or to carry fare-paying passengers*, for which the lien is central to the extension of credit…" *80 FR 37915*. CUAD requests the NCUA to clarify "carry fare-paying passengers" by narrowing the scope to "vehicles solely used to carry fare-paying passengers" or otherwise clarify how vehicles only used part time to carry fare-paying passengers fits into the coverage of commercial loan. For example, how should a family vehicle purchase be classified if the member-borrower is an Uber driver and will use the

family vehicle part-time for carrying fare-paying passengers? CUAD acknowledges the likelihood that the loan to purchase the family vehicle over $50,000 is low, however, in the event the member-borrower already has a commercial loan in which the aggregate could be over the $50,000 threshold.

The proposed rule includes a definition for "residential property" which is proposed to mean, "house, condominium unit, cooperative unit, manufactured home (whether completed or under construction), or unimproved land zoned for 1- to 4- family residential use. A boat or motor home, even if used as a primary residence, or timeshare property is not residential property." *80 FR 37916*. CUAD requests that travel trailers/camper trailers be included within the definition of residential property. Due to shortages in housing in some areas (such as oil fields), and in other areas because of preference, borrowers living in travel trailers/camper trailers may have small businesses for which they are seeking funding and secure this funding by their residence.

A proposed definition for "credit risk rating system" is also included in the proposed rule, which would mean, "formal process that identifies and assigns a relative credit risk score to each commercial loan in a federally insured credit union's portfolio, using ordinal ratings to represent the degree of risk. The credit risk score is determined through an evaluation of quantitative factors based on financial performance and qualitative factors based on management, operational, market, and business environmental factors." *80 FR 37915*. CUAD generally supports a credit risk rating system for credit risk management. The NCUA does further discuss aspects of the "credit risk rating system" in the summary of the proposed rule that is not included in the proposed regulatory language. CUAD requests clear official guidance on what the NCUA will expect to see in a credit risk rating system. As noted above, CUAD implores the NCUA to ensure that the guidance is not counterproductive by reducing the flexibility that this proposed rule would achieve. CUAD again requests that the NCUA allow feedback on any guidance issued to ensure that the message is clear and consistent to both examiners and credit unions.

The NCUA proposed rule significantly expands on the provisions that must be in the credit union's commercial loan policy, previously member business loan policy under existing 723.6. The proposed 723.4 sets forth the minimal requirements that must be included in a board approved, comprehensive written commercial loan policy and establish procedures for commercial lending. CUAD is concerned that the regulatory requirements of what needs to be included in the loan policy may be too extensive for some credit unions with a small MBL/commercial loan program. CUAD recommends that the regulatory requirements for the policy be scaled down to minimal requirements that every credit union must have in its policy regardless of the size of its MBL/commercial loan program. Recommendations for what should be included in policies for credit unions with complex MBL programs can be included in guidance. For example, proposed 723.4(e) which would require that the policy include the, "loan approval processes, including establishing levels of loan approval authority commensurate with the individual's or committee's proficiency in evaluating and understanding commercial loan risk, when considered in terms of

the level of risk the borrowing relationship poses to the federally insured credit union," *80 FR 37916*, should not be a regulatory requirement, but instead a recommendation for larger credit unions with a complex MBL program.

CUAD supports the removal of the waiver requirements. As discussed by the NCUA, "the uniform regulatory prescriptions also inhibit credit unions from considering all relevant risk-mitigating factors in certain borrowing relationships. The current waiver process originally was intended to address case-by-case situations. However, navigating and administering that process requires significant time and resources from both credit unions and NCUA, and can lead to delays in acting on the borrower's application." *80 FR 37899*. CUAD completely agrees with NCUA on this point.

However, with regard to the minimum policy requirements proposed under 723.4(c), a credit union would be required to adopt a policy that includes, "Maximum amount of assets, in relation to net worth, allowed in secured, unsecured, and unguaranteed commercial loans and in any given category or type of commercial loan and to any one borrower or group of associated borrowers. The policy must specify that the aggregate dollar amount of commercial loans to any one borrower or group of associated borrowers may not exceed the greater of 15 percent of the federally insured credit union's net worth or $100,000, plus an additional 10 percent of the credit union's net worth if the amount that exceeds the credit unions 15 percent general limit is fully secured at all times with a perfected security interest by readily marketable collateral as defined in section 723.2 of this part." *80 FR 37916*. This is an area under existing regulations where a credit union could obtain a waiver to exceed these limits, yet, under the proposed rule this would still be essentially a regulatory requirement and a waiver is not available.

CUAD requests that 723.4(c) be revised to require only that the policy include the, "maximum amount of assets, in relation to net worth, allowed in secured, unsecured, and unguaranteed commercial loans and in any given category or type of commercial loan and to any one borrower or group of associated borrowers." To include the additional restrictions/requirements under proposed 723.4(c) without the option of a wavier is more restrictive than what is available to credit unions currently. This aspect of the proposed rule is not providing additional flexibility to credit unions and is unnecessary.

Alternatively, CUAD seeks clarification on whether or not a credit union can provide exceptions to the policy requirement that the, "aggregate dollar amount of commercial loans to any one borrower or group of associated borrowers may not exceed the greater of 15 percent of the federally insured credit union's net worth or $100,000, plus an additional 10 percent of the credit union's net worth if the amount that exceeds the credit unions 15 percent general limit is fully secured at all times with a perfected security interest by readily marketable collateral"? The proposed rule requires, under 723.4(g)(4), the risk management processes, which must be included within the written policy, address, "a process to identify, report, and monitor loans approved as exceptions to the credit union's loan policy." *80 FR 37917*. Within the discussion of the proposed rule, NCUA notes that "the commercial loan policy may allow for exceptions to policy when necessary to meet

the unique circumstances of a borrowing relationship and doing so would not create undue risk to the credit union. The policy must establish the process for approval and documentation of an exception to loan policy. All exceptions to the loan policy need to be tracked and periodically reported to senior management and the board." *80 FR 37907*. If a credit union can make its own internal waiver/exception to the aggregate loan limit to any one member/associated members that is required to be in the policy, then a waiver is not needed, but the NCUA needs to clarify this point.

Proposed section 723.6(c) sets forth the additional policy requirements for construction and development loans. Included among these requirements it that "each loan disbursement is subject to confirmation that no intervening liens have been filed." *80 FR 37917-37918* The NCUA discusses this provision by stating that, "the proposed rule requires a submission of a line-item budget by the borrower and calls for it to be reviewed and accepted by a qualified individual representing the credit union's interest. It outlines the necessary components of the disbursement process that will ensure that funds are disbursed as planned and in accordance with the budget for work completed and to ensure that the collateral protection has not been adversely affected by intervening liens." *80 FR 37908*. CUAD seeks clarification on whether or not each loan disbursement for construction and development loan must be accompanied by confirmation that no intervening liens have been filed or is merely subject to possible confirmation. CUAD is opposed a requirement whereby prior to each loan disbursement for every construction and development loan there must be confirmation that no intervening liens have been filed. Such a requirement is restrictive, inefficient and unnecessary. The credit union should be able to decide based on the individual loan whether or not determinations need to be made regarding intervening liens and with what frequency those determinations need to be made but not every disbursement for every construction and development loan.

The statutory member business loan limits are set forth in proposed 723.8. CUAD fully supports the NCUA proposed rule which betters aligns with the Federal Credit Union Act. Proposed 723.8(a) provides that, "the aggregate limit on a federally insured credit union's net member business loan balances is the lesser of 1.75 times the actual net worth of the credit union, or 1.75 times the minimum net worth required under section 1790d(c)(1)(A) of the Federal Credit Union Act." *80 FR 37918*.

CUAD fully supports the exclusion of "any loan in which a federal or state agency (or its political subdivision) fully insures repayment, fully guarantees repayment, or provides an advance commitment to purchase the loan in full; and any non-member commercial loan or non-member participation interest in a commercial loan made by another lender, provided the federally insured credit union acquired the non-member loans and participation interests in compliance with all relevant laws and regulations and it is not, in conjunction with one or more other credit unions, trading member business loans to circumvent the aggregate limit" from the definition of member business loan. *80 FR 37918.*

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CUAD fully supports the exemptions from the statutory limit of MBLs for, "a federally insured credit union that has a low income designation, or participates in the Community Development Financial Institutions program, or was chartered for the purpose of making member business loans, or which as of the date of enactment of the Credit Union Membership Access Act of 1998 had a history of primarily making commercial loans, is exempt from compliance with the aggregate member business loan limits in this section." *80 FR 37918.* CUAD wants to ensure that any credit unions currently grandfathered in and exempt from the statutory limit for MBLs will continue to be exempt under this proposed rule.

CUAD expresses concern with the bright-line cutoff with regard to the provision, "as of the date of enactment of the Credit Union Membership Access Act of 1998 had a history of primarily making commercial loans." History is made every day and the NCUA should provide the opportunity for credit unions not already exempt from the statutory cap to utilize this exemption after reasonably demonstrating for a period of time a "history of primarily making commercial loans."

CUAD thanks and fully supports the NCUA's intentions to provide credit unions with greater flexibility to meet the needs of the businesses in the communities in which they serve. CUAD believes that the proposed rule is a positive step in achieving this goal and is hopeful that the additional guidance follows this objective.

Thank you for this opportunity to share our comments and concerns.

Respectfully,

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