

December 5, 2013

The Honorable Tom Rice
Chairman
Subcommittee on Economic Growth, Tax and
Capital Access
United States House of Representatives
Washington, DC 20515

The Honorable Judy Chu
Ranking Member
Subcommittee on Economic Growth, Tax and
Capital Access
United States House of Representatives
Washington, DC 20515

Dear Chairman Rice and Ranking Member Chu:

On behalf of the Credit Union National Association (CUNA), I commend you for holding a hearing on examining the post-recession small business lending environment. Credit unions share the Small Business Committee's goal of increasing small business access to capital through the reduction of statutory and regulatory impediments. CUNA is the largest credit union advocacy organization in the United States, representing America's state and federally chartered credit unions and their 98 million members.

As you may know, since their inception in the United States more than 100 years ago, credit unions have been offering business loans to their members. Since 1998, credit unions have operated under a statutory cap on business lending, which limits business lending at most credit unions to 12.25% of assets. Despite this cap, at the end of 2012, credit unions had \$43.2 billion in business loans outstanding. While it is not the primary book of business for most credit unions, it has been the fastest growing type of credit union lending over the last several years.

In fact, bank commercial lending to small businesses (defined as loans less than \$1 million dollars) has fallen from \$756 billion in June of 2007 to only \$653 billion today, a 13.6% decline. Bank loans of this type declined each year for the following five years, according to FDIC data. Meanwhile, credit union lending for member business loans (MBLs) rose from \$26 billion in June of 2007 to \$45 billion today, a 73% increase. As credit unions stepped up and filled the lending void created by banks pulling back in the small business loan arena, credit union market share rose from 3.3% in 2007 to 6.5% today, according to NCUA data.

There is no doubt that there has been a reduction in the demand for business credit as a result of the recession and the slow economic recovery. According to a recent Pepperdine Private Capital Access Index study,¹ 60% of small businesses say the current business financing environment is restricting growth opportunities and 48% of small businesses say the current business financing environment is restricting their ability to hire new employees. However, there is also evidence that a significant contraction in the supply of business credit has contributed to the reduction in credit outstanding.

¹Pepperdine Private Capital Access Index. "PCA Index Survey Responses, Third Quarter 2013". The Graziadio School of Business and Management, Pepperdine University. Presented by: Craig Everett, Ph.D., MBA, Assistant Professor of Finance and Associate Director of the Pepperdine Private Capital Markets Project. Available on the Internet at:
http://3A%2F%2Fbschool.pepperdine.edu%2Fappliedresearch%2Fresearch%2Fpcmsurvey%2Fcontent%2Fq3_2013_pca_index.pdf&ei=CJGgUorcK8ivsATTpIGADA&usg=AFQjCNFFAD8AbhV-iasdiRcebNQgcsQyOg&sig2=dUwscf4NeMNQSA9L6boGXQ&bvm=bv.57155469.d.cWc&cad=rja

For example, according to the Pepperdine survey of U.S. small businesses in the third quarter of 2013, over 59% of small businesses sought a bank loan in the preceding 3 month period, among those fully 56% indicated that they were not successful in obtaining financing. This is a clear indication that a substantial number of small businesses need increased access to capital.

Availability of small business credit is a problem, according to 66% of the businesses surveyed, it is difficult to raise external debt financing. In addition, according to a recent poll commissioned by the American Sustainable Business Council, the Main Street Alliance and the Small Business Majority,² 90% of small business owners believe that the availability of small business loans is a problem, and 60% have faced difficulty trying to obtain loans that would grow their small business. Further, the survey found that 90% of small business owners support making it easier for community banks and credit unions to make loans to small businesses.

The data points referenced above undoubtedly show that businesses want and need access to capital, but are experiencing difficulty and frustration when they approach their financial institution and discover that capital is not easily accessible, even if the business is successful. Credit unions are well capitalized and exist to serve the financial needs of their members. Allowing the free market to function by removing the restrictions on the business lending portfolios of credit unions, will inject more capital in the market place and encourage growth in businesses and the communities in which they operate.

The Credit Union Small Business Job Creation Act

Representatives Ed Royce (R-CA) and Carolyn McCarthy (D-NY) have introduced the Credit Union Small Business Jobs Creation Act (H.R. 688), which would permit well-capitalized, business lending credit unions that have been operating near the current member business lending cap to apply to the National Credit Union Administration for the ability to lend up to 27.5% of their assets to small businesses. We estimate that this bill would allow credit unions to lend an additional \$13 billion to small businesses in the first year, helping them to create 140,000 new jobs at no cost to taxpayers.

The Credit Union Small Business Jobs Creation Act is fully consistent with both the history and mission of credit unions. Credit unions exist to promote thrift and provide access to credit for their members. Since their founding in the United States more than 100 years ago, credit unions have been serving the credit needs of their small business-owning members.

Unfortunately, since 1998, credit unions have been subject to an arbitrary statutory cap on business lending of 12.25% of a credit union's total assets; as a result, today, many credit unions are rapidly approaching the cap while others choose not to engage in business lending because of the cap.

The bank lobby opposes this bill because they oppose credit unions; their arguments are without merit. The bill will not endanger the small banks in your community; the bill will not alter the nature or focus of credit unions; the bill is not inconsistent with the credit union mission or the purpose of their tax status. This legislation recognizes that credit unions are working in their communities to help small businesses and it is important to enact despite opposition by bank lobbyists.

Credit unions understand that in order for the economy to fully recover, small businesses need access to credit, which will help their businesses grow. Credit unions have capital to lend, a history of prudent

² http://www.smallbusinessmajority.org/small-business-research/downloads/012612_Access_to_Credit_Poll_Report.pdf

and safe small business lending and a mission to help provide access to credit to their members – including their small business-owning members.

We also suggest the consideration of several smaller-impact proposals that would facilitate credit union services to their small business-owning members. Some of these proposals have previously passed the House of Representatives.

Treat Non-Owner Occupied One to Four Family Dwelling Loans as Real Estate Loans

As part of the Credit Union Membership Access Act (CUMAA), which imposed the cap on credit union member business lending, Congress included a provision designating loans made by credit unions for non-owner occupied one-to-four family dwellings as business loans, making these loans subject to the member business lending cap. However, if this type of loan is made by a bank, it is treated as a residential loan. We encourage Congress to enact legislation that treats these types of loans when made by credit unions as residential – not business – loans. While it would not have nearly the impact of increasing the credit union member business loan cap, it would give credit unions that are actively managing the cap additional capacity to serve their members with modest rental real estate holdings, and it would bring regulatory parity to the treatment on these loans.

Increase the De Minimus Business Loan Amount

The Federal Credit Union Act exempts business loans equal to or below \$50,000 from the member business lending cap. The de minimus amount has not been adjusted, nor indexed for inflation since 1998.

We encourage Congress to significantly increase the de minimus amount of a credit union business loan and permit the NCUA to adjust this amount no more than once per year to adjust for the effects of inflation. As with the proposal related to one-to-four non-owner occupied dwellings, increasing the de minimus amount would provide credit unions that today are actively managing the credit union member business lending cap the ability to continue to serve their members. Increasing the de minimus to \$500,000 and indexing that amount to take into consideration the effects of inflation would ensure that the loans exempted from the cap are truly small business loans and that the de minimus level, which has not been adjusted in 15 years, adjusts to economic conditions. Even though these loans would not count against the member business lending cap, we would not object to the NCUA having the authority to regulate them for safety and soundness considerations as if they were business loans.

Encourage Small Business Development in Underserved, Urban and Rural Communities

In 2008, the House of Representatives passed legislation, H.R. 6312, the Credit Union, Bank and Thrift Regulatory Relief Act, which included a provision that would have exempted from the credit union member business loan cap a loan made to a business operating in an underserved area. The language envisioned underserved areas as including New Market Tax Credit low-income community areas and Community Development Financial Institution investment areas.

Exclude Member Business Loans Made to Non-Profit Religious Organizations from the Member Business Lending Cap

A handful of very experienced credit unions specialize in making loans to non-profit religious organizations; and these loans are some of the safest loans written today. However, the member business lending cap constrains these credit unions' ability to serve this market, notwithstanding that

the credit unions that originate this lending as generally exempt from the member business lending cap under the grandfather provision enacted in 1998. The reason the cap affects these credit unions is that it is the normal course of business to sell participations of these loans to other credit unions that would be subject to the member business lending cap. Exempting these loans from the cap would permit other credit unions to purchase participations in these relatively safe loans without their parts of the loan counting against the cap. The only change in the treatment of these loans we are proposing affects the treatment under the cap. The participating credit union would still do the necessary underwriting for their portion of the loan; and the loan would continue to be regulated as a business loan, but would exempt it from the risk associated with these loans. We encourage Congress to enact legislation to exempt member business loans made to non-profit religious organizations from the member business lending cap.

Fully Exempt Government Guaranteed Business Loans from the Member Business Lending Cap

Under current law, the guaranteed portion of a business loan made through a government-guaranteed loan program is exempt from the credit union member business lending cap. Many credit unions participate in Small Business Administration (SBA) programs, including the 7(a) loan program. At the end of 2012, there were 347 credit union SBA lenders – collectively they reported \$921 million in SBA loans outstanding in 8,142 individual loans (the average credit union SBA loan size is thus roughly \$100,000). In dollar terms, SBA loans are equal to about 2.1% of total MBLs at credit unions. Since December 2008, the number of SBA loans outstanding has grown 89% at credit unions throughout the nation.

To encourage greater credit union participation in the 7(a) program and to help SBA-lending credit unions have additional capacity to manage the credit union member business lending cap, we encourage Congress to enact legislation that fully exempts loans made through the 7(a) program from the business lending cap. We appreciate that Representative Nydia Velazquez (D-NY) has in the past introduced legislation to this end, and we hope we can work with her and others on this issue.

Enable Full Credit Union Participation in the Section 504 Program

To facilitate credit union participation in the SBA's 504 loan program, we encourage Congress to enact a technical change that would permit credit unions to participate in the government guarantee loan programs on the terms set out in the regulations governing those programs. The regulations governing the 504 loan program permit lenders to take certain action that would otherwise be prohibited for federal credit unions under the Federal Credit Union Act. For example, the Federal Credit Union Act prohibits federal credit unions from imposing prepayment penalties; however, prepayment penalties are permitted by the regulations governing the 504 loan programs. We believe that federal credit unions participating in the 504 loan program should be able to exercise the same powers as other lenders participating in the program, consistent with current regulations. We encourage Congress to enact a technical amendment in this regard, noting that the House of Representatives passed such an amendment as part of the Credit Union, Bank and Thrift Regulatory Relief Act of 2008.

America's credit unions and their 98 million members stand ready to remain part of the solution to the economic problems our nation faces. To that end, we are encouraged by and appreciate your support for increasing the ability for credit unions to better serve their small business-owning members.

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Reduce the Loan Loss Reserve Requirement of SBA's Microloan Program

The SBA's Microloan Program is designed to provide small businesses with short-term loans for working capital or to purchase inventory or supplies. Under this program, the SBA makes special funds available to nonprofit organizations with experience in lending and technical assistance called intermediaries. These intermediaries then make loans to eligible borrowers in amounts up to a maximum of \$50,000.

In order to be an intermediary, the financial institution is required to have a loan loss reserve fund that is 15 percent of the outstanding balance of the notes receivable owed to the intermediary. While there are circumstances where the Administrator may reduce the annual loan loss reserve requirement, in no case will it be allowed to drop below 10 percent of the outstanding balance of the notes receivable owed. In the situations where the Administrator may reduce the loan loss reserve for an intermediary, the average loss rate for the intermediary must be less than 15 percent during the 5 years preceding said period.

We encourage Congress to enact legislation that reduces the loan loss reserve requirement for SBA microloans to no more than 5 percent of the outstanding balance of the notes receivable owed to the intermediary, and authorize the Administrator to reduce the annual loan loss reserve requirement to no less than 1 percent if the average annual loss rate for the intermediary is less than 5 percent.

On behalf of America's 7,000 credit unions and their 98 million members, thank you for your consideration.

Best regards,

A handwritten signature in black ink, appearing to read 'Bill Cheney', with a long, sweeping underline.

Bill Cheney
President & CEO