



Credit Union Member Business Loans

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Summary

The credit union industry has long advocated for relief from statutory restrictions on business lending activities. Credit unions can make loans only to their members, to other credit unions, and to credit union organizations. Specific restrictions on business lending include an aggregate limit on an individual credit union's net member business loan balances and on the amount that can be loaned to one member.

Industry spokesmen have argued that the current economic climate reinforces the argument for regulatory relief from limitations on member business loans. The current financial crisis has resulted in a contraction of credit available to small businesses in most sectors of the U.S. economy. Easing the restrictions on member business lending could increase the available pool of credit for small businesses.

The past two Congresses considered but did not pass legislation providing additional lending authority. The banking industry has generally opposed legislation that would increase the powers of credit unions. Current legislation, the Promoting Lending to America's Small Businesses Act of 2009 (H.R. 3380) and the Small Business Lending Enhancement Act of 2009 (S. 2919) would provide credit unions with expanded business loan authority.

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Background

Overview of the Credit Union System

The original concept of a credit union was of a cooperative organization formed for the purpose of promoting thrift among its members and providing them with a source of low-cost credit. During the past couple of decades, technology, competition, and economic conditions have brought many changes to the financial services marketplace that have affected all types of depository financial institutions. The credit union industry has evolved with marketplace changes so that many of the financial services credit unions provide are similar to those offered by banks and savings associations. Credit unions nevertheless remain distinguishable because of their cooperative framework and unique charter requirements. Credit unions are nonprofit, member-owned financial institutions and are subject to specific restrictions not placed on other depository financial institutions. Given that credit unions are considered financial cooperatives, the institutions are exempt from federal income tax. Individual members are taxed on their dividends.

Credit union charters are granted by federal or state governments on the basis of a “common bond.” This requirement determines the field of membership, and it is unique among depository financial institutions. There are three types of charters: (1) a single common bond (occupation or association based); (2) multiple common bond (more than one group each having a common bond of occupation or association); and (3) a community-based (geographically defined) common bond.

Individual credit unions are owned by their membership. The members of a credit union elect a board of directors from their institution’s membership (one member, one vote). Members’ savings are referred to as “shares” and earn dividends instead of interest. Credit union loan and investment powers are more restricted than those of commercial banks. Credit unions can only make loans to their members, to other credit unions, and to credit union organizations. The investment authority of federal credit unions is limited by statute to loans, government securities, deposits in other financial institutions, and certain other limited investments.

The National Credit Union Administration (NCUA), an independent federal agency, is the federal regulator for credit unions. The National Credit Union Share Insurance Fund (NCUSIF) is the federal deposit insurance fund for credit unions. The NCUA manages the NCUSIF for the credit union industry. As of December 31, 2008, there were 7,806 federally insured credit unions. These federally insured institutions held assets totaling \$811.2 billion.

Member Business Loans

As mentioned above, a credit union’s lending authority is limited to loans to its members, to other credit unions, and to credit union organizations. The definition for member business loans was codified in 1998 by P.L. 105-219¹ (the Credit Union Membership Access Act). A member business loan is any loan, line of credit, or letter of credit used for an agricultural purpose or for a commercial, corporate, or other business investment property or venture. The definition of a member business loan excludes loan(s) of up to \$50,000 to one member-borrower. Additionally,

¹ 112 Stat. 920.

the aggregate amount of outstanding business loans to one member or group of associated members is limited to a maximum of 15% of the credit union's net worth or \$100,000, whichever is greater. P.L. 105-219 placed additional restrictions on this type of lending. The aggregate amount of member business loans made by a credit union is restricted to the lesser of 1.75 times the credit union's net worth or 12.25% of the credit union's total assets. Three exceptions to the loan limit are authorized: (1) credit unions that have low-income designation or participate in the Community Development Institutions program; (2) credit unions chartered for the purpose of making business loans (as determined by the NCUA); and (3) those with a history of primarily making such loans (as determined by the NCUA).

The volume of credit union member business lending has increased over time, but member business loans continue to account for a small portion of total lending. From December 2004 to December 2008, total member business loans grew from \$12.3 billion to \$30.1 billion. In December 2004, member business loans accounted for 3% of all credit union lending, and in December 2008, member business loans accounted for 5.3% of total loans.²

Legislation and Policy Issues

Current Legislation

The credit union industry has for several years sought relief from the restrictions placed on member business loans by the Credit Union Membership Access Act. In the 110th Congress, provisions to ease credit union lending restrictions were introduced but not passed. Provisions to increase credit union lending authority were included as part of omnibus regulatory modernization legislation for credit unions, the Credit Union Regulatory Improvements Act (CURIA).³ Current legislation focuses solely on member business lending. On July 29, 2009, the Promoting Lending to America's Small Businesses Act of 2009 (H.R. 3380) was introduced, by Representatives Paul E. Kanjorski and Edward R. Royce, and referred to the House Committee on Financial Services. On December 21, 2009, the Small Business Lending Enhancement Act of 2009 (S. 2919) was introduced, by Senators Mark Udall, Charles E. Schumer, Joseph I. Lieberman, Olympia Snowe, Barbara Boxer, Susan M. Collins, and Kirsten E. Gillibrand, and referred to the Senate Committee on Banking, Housing, and Urban Affairs. The intent of both bills is to increase the availability of credit for small businesses and thereby create jobs by providing credit unions with expanded loan authorities. An overview of the provisions of H.R. 3380 and S. 2919 follows below.

Provisions contained in both bills:

- The bills would raise the limit on the aggregate amount of member business loans made by a credit union. It would replace the language restricting the lending to the lesser of 1.75 times the credit union's net worth or 12.25% of the credit union's total assets with a flat level of 25% of total assets.

² See <http://webapps.ncua.gov/ncuafpr/>.

³ For information on legislation in the 110th Congress, please see CRS Report RS22661, *Credit Union Regulatory Improvements Act (CURIA): H.R. 1537 and S. 2957*, by Pauline Smale.

- The definition of a member business loan currently excludes loan(s) of up to \$50,000 to one member-borrower. H.R. 3380 and S. 2919 would change this to exclude loan(s) up to \$250,000.

The next set of provisions are only covered by H.R. 3380:

- Currently, an insured credit union that is undercapitalized⁴ may not make any increase in the total amount of member business lending outstanding at that credit union until the credit union becomes adequately capitalized. The legislation would give the NCUA the authority to waive this restriction and permit the undercapitalized credit union to continue to make new member business loans. The NCUA would have the authority to oversee the member business lending of an undercapitalized institution.
- The member business loan limit would no longer apply to loans to, or loan participations by, nonprofit religious organizations.
- H.R. 3380 would also exclude member business loans made in underserved urban and rural communities. These underserved areas include “investment areas” under the Treasury Department’s Community Development Financial Institution (CDFI) program and qualified “low-income areas” under the New Markets Tax Credit Targeting formula adopted by Congress in 2000.⁵ Census tracts that would otherwise qualify but in which more than 50% of resident families make more than \$75,000 per year would not qualify. In addition, provisions would make a distinction between loans made to businesses operating on a nationwide basis (these would not qualify for exclusion) and loans made to locally owned franchises (operating in an underserved area) of businesses operating on a nationwide basis (these would qualify for exclusion).

The following provision is only found in S. 2919:

- The legislation would require the NCUA to submit semiannual reports to Congress on the status of member business lending. The report would include information on the types and amounts of member business loans, trends in lending, and any recommendations for legislation.

Policy Issues

Credit union advocates have argued that easing the limitations on member business lending would allow credit unions to better serve their membership while enhancing small business formation and growth. In addition, they suggest that current economic circumstances and the general contraction of available credit strengthen the argument for such measures. Banking industry advocates have generally opposed any legislation that would provide credit unions with expanded powers.

Credit union advocates argue that changing the current statutory restrictions on member business lending would increase the opportunity for credit unions to serve their business-owning members.

⁴ Defined by Section 216(g)(2) of the Federal Credit Union Act (12 U.S.C. 1790d(g)(2)).

⁵ The New Market Tax Credit program was created by the Community Renewal Tax Relief Act of 2000 which was passed as part of Title I of the Consolidated Appropriations Act of 2001 (P.L. 106-554, 114 Stat. 2944).

Advocates claim that the current limits deter individual credit unions (especially smaller institutions) from entering into member business lending because the volume of loans needed to offset the costs of starting and operating a member business loan program often cannot be achieved under the current limits and restrictions. Because the business lending authority would still be limited to members, advocates of easing restrictions claim that this would not undermine the founding principles of credit unions.⁶

Banking industry advocates have raised concerns that greater lending authority for credit unions would unfairly enhance the competitive strength of the latter if credit unions retain their federal income tax exemption.⁷ The distinctions between credit unions and banks (especially community banks) have arguably become increasingly blurred. Competition issues may thus arise if credit unions are granted additional bank like powers without being subjected to the same laws and regulations as banks.⁸

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⁶ For more information on arguments in support of easing member business lending restrictions, please see a letter to Members of Congress from the Credit Union National Association, which can be found at http://www.cuna.org/download/congress_letter_120809.pdf.

⁷ For a discussion of this issue, please see CRS Report 97-548, *Should Credit Unions Be Taxed?*, by James M. Bickley.

⁸ For more information on the concerns of the banking industry, please see a letter to Members of Congress from the Independent Community Bankers of America, which can be found at <http://www.icba.org/files/ICBASites/PDFs/ltr011410.pdf>.