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Small Businesses Find a New Source for Funding
By JILIAN MINCER

Unable to get loans at banks, more small-business owners are turning to credit unions.

Most credit unions didn't get in on the subprime-loan market, so they're not smarting from multibillion-dollar losses like many banks. Many also have extra cash because deposits increased in 2008 as more investors abandoned the stock market and sought greater certainty in savings accounts. So credit unions are more able -- and willing -- than most of their banking counterparts to dole out money to small businesses.

Matt Rosenthal, vice president of business services of Summit Credit Union, right, with Josh Duggan, president of Chem-Dry of Madison. Mr. Duggan received two business loans from Summit Credit Union.

About 27% of the 8,147 credit unions in the U.S. offer business loans, according to the Credit Union National Association, a trade group based in Washington, D.C. The amount of business loans was up 18% last year to almost \$33 billion from nearly \$28 billion in 2007. The average loan size is about \$215,000.

"In this really bad environment, we're doing more and more loans," says Mike Schenk, senior economist at the Credit Union National Association.

Many credit unions say they would lend out even more money if they could. But a 1998 federal law caps the amount of business loans credit unions can have at 12.25% of assets. The banking industry opposes any changes to the legislation, but credit unions hope to convince Congress to introduce legislation to lift the cap. Last year, a bill was introduced to raise the lid to 20%, but it didn't garner enough votes.

"We believe credit unions could provide \$10 billion in small-business loans within the next 12 months without costing taxpayers a nickel," if there wasn't a cap, says Larry Wilson, president and chief executive of the Coastal Federal Credit Union in Raleigh, N.C., which is about \$5 million from hitting the 12.25% limit. It has a total \$250 million in loans on its books.

Mr. Wilson says without the limit, Coastal alone could make about \$165 million more in loans to small companies over the next 12 months. He says the 189,000-member credit union is processing \$39 million in loans right now and is in the beginning stages of another \$55 million in loans.

Credit unions are chartered as nonprofit cooperative institutions owned by their members. Like other financial institutions, however, they are regulated, and deposits of up to \$250,000 are insured.

Kenneth Beine, president and CEO of Shoreline Credit Union in Two Rivers, Wis., says the credit union has seen more "Main Street" loans coming to them as traditional sources of funding have dried up. Last year, Shoreline made \$10 million in business loans, up from less than \$1 million a year earlier, without advertising.

Mr. Beine says because of the demand, the credit union hired another person with commercial-lending expertise. He says the average loan is for less than \$100,000 -- most often for small companies or home-office businesses that banks aren't interested in lending to.

Mr. Beine adds that "we could easily do twice as many loans. But by mid-2009, we'll be bumping the limit." Shoreline has about \$90 million in assets and more than 10,000 members.

Josh Duggan, president of Chem-Dry of Madison, decided last year to apply for loans at the Summit Credit Union in Madison, Wis., because he wanted to grow his carpet and upholstery cleaning business and wasn't happy with the service he was getting at the bank. He ended up getting two loans, one for \$21,000 and the other for \$18,000, for a vehicle and equipment.

Matt Rosenthal, vice president of business services at Summit Credit Union, says unlike some banks, the credit union has money to lend because it didn't lend to some of the real-estate developers that are now suffering. The credit union's average loan is \$250,000 to \$350,000.

Nick Frescas qualified for a \$150,000 loan from West Texas Credit Union in El Paso after his family's home day-care business, Grammies Day Care and Learning Center, failed to get a bank loan in 2005. He says the bank told him the business didn't have enough assets. Grammies Day Care is now in the process of applying for a \$750,000 20-year loan to buy the building where its second day care center is located.

While the credit unions are lending, some are demanding more proof of income from borrowers. Curtis Anderson, vice president at Mountain America Credit Union in West Jordan, Utah, says it has "changed its underwriting criteria in small ways." For instance, it now requires potential borrowers to verify their income with tax forms, pay stubs and other forms. Before, the credit union would simply accept stated income on an application.

But even with the slightly tightened requirements, Mountain America continues to lend to individuals starting businesses. "We're one of the only solutions for a start-up, and we want to be part of that," Mr. Anderson says.

Mr. Schenk of the Credit Union National Association says the federal cap discourages many credit unions from even offering business loans because "it's expensive to start up a business-loan department." Credit unions are required to hire experienced loan officers if they are going to provide business loans.

"The 12.25% placed on credit unions is an arbitrary cap that was imposed in 1998 as part of the Credit Union Membership Access Act," says Mr. Schenk. He says that historically there were no restrictions on credit union business lending. The credit unions are owned by their members "so it is not about maximizing its profits, it's about maximizing service."

Keith Leggett, a senior economist at the American Bankers Association, says credit unions were established to serve "people of modest means" and should focus on consumers. Changing the 12.25% lid "would allow them to venture into making larger commercial loans," which may give credit unions -- which are tax exempt -- an unfair advantage over "the community banks that they are competing with for customers," he says.