

Pathways

Financial Credit Union

House Financial Institutions, Housing, and Urban Development Committee

Interested Party Testimony
H.B. 67

Greg Kidwell, President
Pathways Financial Credit Union

May 2, 2017

Chairman Dever, Vice Chair Sprague, Ranking Member Smith, and members of the House FIHUD Committee, on behalf of the nearly 27,500 members of Pathways Financial Credit Union, I want to thank you for the opportunity to provide interested party testimony for HB 67, changing the requirements for confessions of judgment.

My name is Greg Kidwell and I am the President of Pathways Financial Credit Union. As a \$246 million credit union with seven branch locations throughout Central Ohio, Pathways was formed through a strategic merger of three mid-sized, \$50 to \$60 million credit unions in 2012. The purpose of that strategic merger was to enable Pathways to more efficiently and effectively serve the needs of our members, which consist of both consumers and small businesses. I would also like to note that I am in my final term of volunteer service to the State of Ohio as an appointed member of Credit Union Council.

Pathways Financial Credit Union is one of the 126 Ohio credit unions offering commercial loans, engaged in what we call "member business lending" to our members. Today, Pathways serves a group of over 700 business members, who in aggregate have nearly \$20 million on deposit with the credit union, and whose aggregate member business loans outstanding total over \$5.9 million.

As entities participating in member business lending, credit unions include cognovits within each member business loan originated as a tool of last resort. While it is in the best interest of the lender and small business that a loan be fulfilled through payment or other means of resolution, a credit union would only execute a confession of judgment in extreme monetary or non-monetary default situations.

Ohio's credit unions appreciate the open dialogue with the bill sponsor, Representative Young, and his efforts to alleviate issues pertaining to limiting cognovits and extensive borrower notification. However, there are a few additional considerations I would like to highlight to the committee that may produce unintended consequences should the bill in its current form be approved.

First, there needs to be lender protection inserted into this bill in terms of loss of/missing/impaired collateral. Take for example a rather common scenario: a commercial loan collateralized by equipment and machinery. In the case of non-titled collateral, the lender would file a UCC lien on these assets at

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the time that the loan was made. However, a UCC lien will not stop the borrower from selling such assets in a casual sale, or putting them up for sale on e-Bay, for example. And if that happens, a lender is without the ability to obtain a cognovit judgment immediately because loss of collateral is a non-monetary default. Hence, where collateral goes missing, a credit union has to sue, wait at least 28 days for service, and engage in full litigation with a borrower who has misappropriated collateral. Instead, if the lender learns of the sale, or the pending sale, of the collateral prior to a monetary default, the lender should have the right to use cognovit terms to obtain immediate judgment.

Additionally, the bill should include lender protection in terms of non-monetary default situations such as the failure of a business to meet the covenants of a loan, for example, cash flow significantly below the covenant amount or, even negative cash flow, or violation of a covenant to subordinate other debts, or not borrow additional funds without the consent of the original lender. Violation of some covenants can cause regulatory issues for Ohio's lenders as well. Issues with loan-to-value ratios, cash-flow covenants, and a borrower's financial condition can downgrade the quality of a loan in the eyes of regulators, which can result in financial and other penalties for Ohio's credit unions. Hence, monetary defaults are not only the only defaults that cause financial loss to the lender.

Loan covenants are also an important tool for commercial lenders, and when a borrower starts to violate covenants, speed is often the key in terms of securing a meaningful recovery of the loan proceeds from the lender's standpoint, before the point of monetary default.

Finally, I feel that lender's rights in terms of cross-default should also be preserved as well. Say you have two commercial loans with my credit union. One is secured by commercial real estate, and the other is an unsecured line of credit. Now, let's say you are experiencing severe cash flow issues. If you are paying the building loan in a timely manner in order to avoid losing the real estate, but you are severely delinquent on the line of credit, the credit union in this case should have a right to declare cross-default on the building loan in order to mitigate to the best extent possible the loss on the delinquent line of credit.

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Hopefully, these examples will represent to you that the cognovit judgment is used strictly as a defensive tool by Ohio credit unions, and used only in cases where the credit union's prospects for recovery of the members' funds that were lent to the borrower have been severely limited by monetary or non-monetary default.

In closing, credit unions remain responsible small business lenders who prioritize the financial well-being of Ohio's nearly 3 million members. By limiting the use of cognovits in a manner that neglects to strike a balance between lender and borrower rights, HB 67 could provide unintended consequences for credit unions offering business loans in terms of their ability to offer accessible and affordable capital to members and your constituents.

Thank you again for the opportunity to provide interested party testimony today and I would be more than willing to discuss ways to strengthen HB 67 with the sponsor and committee members. I also would be happy to answer any questions you may have at this time.