



STATE OF INDIANA

DEPARTMENT OF FINANCIAL INSTITUTIONS



30 South Meridian Street, Suite 300
Indianapolis, IN 46204
Telephone: (317) 232-3955
FAX: (317) 232-7655
WEB SITE: <http://www.dfi.state.in.us>

May 19, 2016

To: All Financial Institution Chief Executive Officers, Managers, and Presidents

Re: Applicability of the State's legal lending limit statutes to Bankers Healthcare Group loans

The prolonged low-interest rate environment, highly competitive local markets, and the expansion of non-depository lending firms has resulted in institutions exploring more non-traditional avenues to diversify and grow their balance sheets as a supplement to the traditional organic means. Loans obtained through third-party relationships can be a beneficial tool when looking to expand and diversify the loan book, assuming prudent risk management practices are employed throughout the lifecycle of the lending relationship. Risks such as compliance, operational, concentration, vendor, and legal risks should all be considered in conjunction with the typical credit risk determination process. As the universe of third-party products evolves, the Department continuously evaluates risks associated with each product identified during our routine examination reviews. The Department has recently reviewed the applicability of the State's legal lending limit for credits garnered through certain third-party relationships, with a particular focus on programs that include credit enhancements which may retain an interest or control in the relationship by the original lender. The legal lending limit statute applicable to banks is cited in IC 28-13-1.5 and to credit unions in IC 28-7-1-39.

The Department has witnessed significant growth in certain third-party lending programs in recent years, resulting in an enhanced review process in 2015 to determine aggregation requirements for lending limit purposes. The review identified the Bankers Healthcare Group (BHG) relationships as having several unique characteristics. Extensive review of the relationship was conducted during on-site examinations, additional discussions with individual institutions, and through nationwide regulatory conference groups. Loans purchased from BHG are relatively small dollar, and are generally originated for working capital to healthcare professionals in the United States. In addition to working capital loans, BHG originates loans for debt consolidation; expansion and improvement; equipment financing; and practice acquisition needs. These loans are originated to new and existing practices, with often thin marketable collateral. Loans can be obtained through private placement, an online auction process, and through a joint venture program. Loans originated by BHG often times carry a significantly higher interest rate compared to what is passed through to the participant institution, thus the institution could be considered to be purchasing a cash flow stream rather than the actual loan.

It is the Department's interpretation that loans obtained from BHG should be aggregated for compliance with the lending limit statutes if they have all or any of the following caveats. While the loan master agreements between BHG and the institution indicate that these loans are "sold" to the subject financial institution, and underwritten on an individual basis by BHG, the agreement gives BHG interest and/or control in the credit after "sale" in the form of collection, the ability to substitute loans in the event of default, and the ability of BHG to negotiate prepayment terms with the borrower. It is the Department's opinion that the existence of the aforementioned clauses in the contract does not fully eliminate control and maintains an interest in the loan post participation by BHG. Commonality in repayment appears to exist in the event of default, as BHG is serving as a secondary source of repayment given their authority to serve in a collection capacity upon notification within the defined timeframe and their option to substitute loans on request. BHG holds the right to substitute on request, not the institution, thus giving BHG control in the repayment process. Additionally, BHG's ability to negotiate prepayment terms on behalf of financial institution evokes another level of control. Given the aforementioned control in which BHG retains throughout the lending relationship and the commonality of repayment characteristics, loans obtained from BHG should be aggregated when considering the limitations established in IC 28-13-1.5 and IC 28-7-1-39.

The Department is aware that specific financial institutions currently have holdings of BHG loans in excess of the lending limit statutes. The Department will not penalize institutions, through the formal citation of a violation in their next examination report, that have concentrations in excess of the limits established as of the date of this letter. However, the Department would request that each of these institutions, prior to calendar year-end 2016, develop a plan to achieve compliance with the thresholds established, within a reasonable period of time.

The Department understands that new third-party lending programs are continually developed and existing programs evolve. The Department will evaluate lending programs from BHG, or other third-party lenders, for compliance with the legal lending limit as questions arise. Please direct any questions or concerns to Christopher Dietz, Assistant Regional Field Supervisor, 317-617-8440, cdietz@dfi.in.gov or Mark Powell, Credit Union Division Supervisor, 317-232-3955, mpowell@dfi.in.gov.



Thomas C. Fite
Director
Indiana Department of Financial Institutions