

March 19, 2004

Kenneth E. Ackerman, Esq.  
McKenzie Hughes LLP  
101 South Salina Street  
Syracuse, New York 13221-4967

Re: No-Interest Loans to Nonprofit Community Organization.

Dear Mr. Ackerman:

You have asked if a federal credit union (FCU) may provide no-interest loans to a nonprofit corporation that administers a community home loan program. Yes, an FCU may provide no-interest loans under its incidental powers authority to make charitable contributions.

Your FCU clients would like to make direct donations and no-interest loans to Home Headquarters, Inc. (HH), a not-for-profit organization that administers the Syracuse Neighborhood Initiative Home Improvement Loan Program. The loan program is capitalized by funds HH has received from various sources including the NYS Home Program, the Neighborhood Reinvestment Corporation, the US Treasury Department (CDFI Core Fund) and the Affordable Housing Corporation. Under the program, loans are made to families for home repairs. These prime rate loans average \$10,000 and are made for terms up to seven years. HH takes the applications, qualifies borrowers, processes paperwork, collects payments, and follows delinquencies. Your FCU clients each would "lend" HH \$125,000 for seven years but the "loans" would be unsecured and HH will pay no interest and repay only 95% of the principal amount. In effect, the FCUs are donating 5% of the "loans" and the use of their funds for a period of seven years.

NCUA has long recognized an FCU's authority to make charitable contributions and donations under the conditions in its charitable donations rule. 12 C.F.R. §701.25; See 64 Fed. Reg. 19441 (April 21, 1999). An FCU may make charitable contributions to nonprofit recipients that are located or conduct activities in a community in which the FCU has a place of business. 12 C.F.R. §701.25(a). An FCU's board must approve charitable donations and may only approve donations that are in the best interests of the FCU and reasonable given the size and financial condition of the FCU. 12 C.F.R. §701.25(b).

We believe an FCU of sufficient size and in good financial condition can make an interest-free loan to an appropriate recipient as a charitable contribution under NCUA's charitable donations rule. 12 C.F.R. §701.25. An FCU's board of directors is in the best position to decide if it is reasonable and in the best interests of the FCU to donate money to a nonprofit organization in its community. We believe that, if an FCU can donate money to its community's nonprofits, it can lend money as described above without such donations being classified as loans.

Under the incidental powers analysis, an FCU may donate the use of funds over time to an appropriate recipient as a permissible incidental powers activity. 12 C.F.R. §721.2. These donations are useful in carrying out the mission of credit unions because this type of charitable giving can promote name recognition and generate goodwill in the FCU's community. As the functional equivalent of direct contributions to community nonprofits, these donations pose the same risks to an FCU based on the appropriateness of the donation for the donor.

By donating the use of funds to a nonprofit organization in its community, an FCU is making a charitable donation under its incidental powers authority, and, for regulatory purposes, the donation is not considered a

loan. We believe, therefore, it is irrelevant whether HH is a member or nonmember because your clients would not be making loans to HH. Instead, the FCUs would provide permissible charitable donations to a nonprofit recipient located in a community in which they both have a place of business.

An FCU can account for its donation of the use of money over time by: (1) expensing the 5% donation when made; (2) recording the amount to be paid back (net of 5%) as a receivable; and (3) recording both an income and expense in increments over the course of the agreement to capture both the “earning” of income on the loan, and the expensing of the same as a contribution.

This opinion recognizes an FCU’s authority to make charitable contributions in the form of interest-free loans when the donation meets the FCU’s charitable giving goals and is both reasonable and in the best interests of the FCU. FCUs may not use this authority to circumvent the Federal Credit Union Act, which limits an FCU’s lending to members, or NCUA’s regulations governing loans or member business loans.

Sincerely,

Sheila A. Albin  
Associate General Counsel

OGC/CJL:bhs  
04-0139