



State of Washington

**DEPARTMENT OF FINANCIAL INSTITUTIONS
DIVISION OF CREDIT UNIONS**

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May 14, 2010

“A” CEO
“B” Credit Union

DCU Interpretive Letter I-10-03

Subject: Investment in Real Estate

Dear “A”:

In October 2009, you inquired about whether or not it was permissible for “B” to offer a long-term lease on a parcel of land to allow development. The parcel has a standalone branch, but the branch does not use the full plot. I called you back in October 2009 and told you verbally that, under the Washington Credit Union Act (“the Act”), Washington credit unions are not permitted to own real estate for investment purposes beyond use for their own operations. RCW 31.12.438. I told you that I would send a formal letter with my research information on a later date. I apologize for the delay in sending you this formal response.

Credit unions are only permitted to exercise powers granted to them under the Act. These may come from three sources: 1) enumerated, general powers; 2) incidental powers granted under the Act; or 3) powers granted to federal credit unions and extended to state credit unions by the Act’s parity clause. Each potential source of authority will be addressed in turn.

1) Enumerated Powers

A credit union’s general powers are laid out in RCW 31.12.402. The most relevant provision, subsection (6), permits a credit union to “[a]cquire, lease, hold, assign, pledge, sell or otherwise dispose of interests in . . . real property in accordance with RCW 31.12.438.” In turn, RCW 31.12.438 authorizes a credit union to invest in real property “primarily for its own use.” In recognition of the fact that credit unions occasionally have property or office space that they cannot fully utilize, in 1998 the Department of Financial Institutions (“DFI”) opined that this

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provision would permit a credit union to lease some portion of its property to another person

or entity, so long as the credit union continued to use 50% plus one square foot of the property. See redacted Opinion Number 98-3. This interpretation would not, however, extend to permit development or leasing of additional property bought for speculative purposes or a parcel split off of an existing property. There are two exceptions to the real estate investment limitation that could authorize a credit union to lease property to generate income.

The first exception is regarding property acquired for future expansion. Under RCW 31.12.438 (2), a credit union may acquire land for future expansion. The credit union must use the property within three years of purchase. Even assuming that “B” has held the property for less than three years, this exception does not appear to apply because “B” is seeking a long-term lease for non-credit union uses, not to retain the property for “B’s” future expansion. If “B” believes in good faith that it would use the additional parcel for operations within three years of its original purchase, then it would be permitted to split and hold the new property. That does not appear to be the case.

The second exception from the restriction against investment in property is for situations where the director waives the limitations of RCW 31.12.438. The Director has delegated this authority to the Division of Credit Unions. Because of the potential risks to the credit union system if credit unions were permitted to purchase or use their property for speculative purposes or in order to produce income, the Division of Credit Unions is not inclined to grant such waivers. To grant a waiver in this instance would be to run counter to the intent of the legislature in adopting the Act, and would be a potentially dangerous precedent.

2) Incidental Powers under the Act

Credit unions are provided with incidental powers. RCW 31.12.402 (23) provides that credit unions may “[e]xercise such incidental powers as are necessary or convenient to enable it to conduct the business of a credit union.” Since 2001, DFI has directed credit unions to seek approval of any activity under this clause unless the activity is on the National Credit Union Administration’s (NCUA) preapproved list or the activity has been approved in writing by either the NCUA or DFI. The preapproved list is available in 12 C.F.R. § 721.3.

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The NCUA considers an incidental power activity as one that “is necessary or requisite to enable you to carry on effectively the business for which you are incorporated.” 12 C.F.R. § 721.2. The list of preapproved activities in 12 C.F.R. § 721.3 includes twelve specific activities. The one that appears to be most relevant is:

(d) *Excess capacity*. Excess capacity is the excess use or capacity remaining in facilities, equipment, or services that: You properly invested in or established, in good faith, with the intent of serving your members; and you reasonably anticipate will be taken up by the future expansion of services to your members. You may sell or lease the excess capacity in facilities, equipment or services such as office space, employees and data processing.

(Emphasis added). While there has been no suggestion that “B” improperly invested in the parcel, “B” does not appear to reasonably anticipate credit union expansion to require use of 50% plus 1 square foot of the parcel to be split and developed. What “B” has proposed to do is not to lease excess office space, but to offer a long-term lease in order to generate income. In fact, the long-term lease contemplated by “B” would make it unlikely that space would be available if expansion became necessary.

For the reasons above, “B”’s proposed use would be beyond the incidental powers provided by subsection (d). This kind of activity is clearly not “necessary or requisite” to enable “B” to carry out its business as a credit union, and would only be permitted as an incidental power if either DFI or NCUA authorized it in writing. No evidence suggests that either have, so “B” cannot offer its proposed long-term lease on its property as an incidental power.

3) Parity Powers

RCW 31.12.404 grants state credit unions the powers possessed by a federal credit union between December 31, 1993 and July 22, 2001. They may also have powers possessed by federal credit unions at a later date if such powers are approved by DFI. This provides both enumerated powers and incidental powers. Federal incidental powers are addressed above.

Federal credit unions are permitted to “purchase, hold, and dispose of property necessary or incidental to its operations” under 12 U.S.C. 1757(4). This is similar to the restrictions in the Act. The NCUA has reviewed requests much like the one made by “B”. In a 1991 letter, the NCUA addressed a situation in which a credit union wished to enter into a fifteen year lease regarding an unfinished building on the property that included its headquarters. The NCUA declined to authorize such a lease. Kevin L. Johnson Letter. In a 2006 letter, NCUA defined “operations” of a credit union to include only “providing financial products and services to members.” Michael D. Lozoff Letter. “B”’s proposed use is outside of those operations, and would not be permitted for a federal credit union.

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DFI has been unable to find any evidence that federal credit unions are permitted to engage in the type of activity contemplated by “B” in the current situation. In fact, a Pennsylvania credit union association requested the ability to conduct these kinds of activities during proposed NCUA rulemaking in 2008. The rulemaking was ultimately not undertaken, leaving federal credit unions unable to make such purchases. Absent a showing that federal credit unions can engage in these kinds of transactions, DFI has concluded that Washington credit unions have no authority under the parity provision to make long-term leases of property to produce income.

Conclusion

If “B” elects to continue with its plan to split the unused piece of the parcel from the one used for the standalone branch, it must either sell the undeveloped parcel no more than three years after its initial purchase of the larger parcel, or seek a waiver from DFI under the Act. If “B” chooses to retain both the developed and undeveloped pieces of the property as one parcel, it may continue to own the property as long as it is used primarily for credit union purposes.

While we are not unsympathetic with your situation, and understand that you believe a long-term lease of your excess property for commercial purposes would be in the best interest of your members, it is not permitted under the Act. The Division of Credit Unions will not grant a waiver of the relevant provisions of law at this time. If you have any additional questions, please contact me at 360-902-8778.

Sincerely,

/S/

Linda Jekel
Director of Credit Unions