

January 19, 2007

Robert K. Rusch, Vice President & Associate General Counsel
CUNA Mutual Group
5910 Mineral Point Road
Madison, WI 53701-0391

Re: Split Dollar Life Insurance and Nonpreferential Loans.

Dear Mr. Rusch:

You have asked if NCUA's rule prohibiting a federal credit union (FCU) official from receiving a preferential loan prevents credit unions from funding an employee benefit plan obligation to an official with collateral assignment split dollar life insurance. 12 C.F.R. §701.19, 12 C.F.R. §701.21(d)(5). No, it does not because the prohibition on preferential loans applies to volunteers, not compensated employees.

NCUA's lending rule prohibits preferential treatment of FCU officials and defines official to mean any member of the board of directors, credit committee or supervisory committee. 12 C.F.R. §§701.21(d)(2), 701.21(d)(5). Among other things, the lending rule states the "rates, terms and conditions on any loan or line of credit either made to, or endorsed or guaranteed by . . . an official . . . shall not be more favorable than the rates, terms and conditions for *comparable* loans or lines of credit to other credit union members." 12 C.F.R. §701.21(d)(5) (emphasis added). Nothing in NCUA's rules prohibits preferential loans to FCU employees who are not officials of the credit union.

NCUA's employee benefits rule exempts an FCU from the investment restrictions of the FCU Act and NCUA rules when it invests under its authority to provide and fund employee benefits. 12 C.F.R. §701.19. Specifically, an FCU may purchase an otherwise impermissible investment to fund an employee benefit plan obligation as long as, among other regulatory limits, there is a direct relationship between the investment and the employee benefit plan obligation it serves to fund.

Split dollar life insurance is a valuable tool for funding employee benefit plans used to attract and retain senior managers and employees; the Office of General Counsel has stated FCUs may purchase split dollar life insurance for this purpose. OGC Op. 05-0117 (January 13, 2005). Split dollar life insurance arrangements can be structured in a number of ways, including an arrangement known as "collateral assignment split dollar life insurance." Under this arrangement, an employee owns the insurance policy and the credit union pays the premiums and, in compliance with Internal Revenue Service regulations, it is structured as a loan to the employee from the credit union for which the employee assigns collateral as security. To the extent a loan is created, the Financial Accounting Standards Board requires employers to record loans receivable from employees with split dollar arrangements.

Sometimes, a CEO or other top executive of a credit union also holds a seat on the board of directors, serving in that capacity as a volunteer official, and we do not believe the limitations of §701.21(d)(5) apply to a loan to an executive under these circumstances. Those limitations are intended to prevent FCUs from making unsafe loans to officials and compensating voluntary officials otherwise prohibited from being compensated. In a previous rulemaking that led to the current language in §701.21(d)(5), NCUA stated:

The granting of loans with preferential rates, terms, and conditions has been used as a way to otherwise compensate officials who could not legally be compensated. The . . . prohibition effectively limits such circumvention. The Board believes that the limitation is necessary because loans underwritten to officials with rates, terms, and conditions that are out of line with the credit union's normal lending policies often result in losses to the credit union. The Board considers this type of lending to be unsafe and unsound

51 Fed. Reg. 46869 (December 29, 1986). NCUA's concern in this rulemaking was about loans to volunteers, not a loan to a compensated executive that is part of an employee benefit plan.

Furthermore, the prohibition in §701.21(d)(5) is limited to preferential treatment of "officials" for "comparable" loans available to other credit union members. Loans that are part of an executive compensation program are not "comparable" loans available to members and this fact further supports our position that §701.21(d)(5) does not apply to a loan to a paid executive as part of a collateral assignment split dollar life insurance arrangement used to fund an employee benefit plan under §701.19.

Please contact Staff Attorney Frank Kressman or me with any additional questions.

Sincerely,

/S/

Sheila A. Albin
Associate General Counsel

GC/FSK:bhs
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