

FYI

M E M O R A N D U M

October 23, 1991

TO: Charles L. Short, Director
Department of Family Resources

FROM: Marc P. Hansen *Marc Hansen*
Senior Assistant County Attorney

RE: County Loan Guarantee for Non-Profit Corporations

Under Chapter 23B, Montgomery County Code (1984), the County is authorized to give financial assistance to a qualified, non-profit corporation. The non-profit corporation must show, inter alia, that financial assistance from the County is necessary to ensure the continued operation of the organization. You stated in your memorandum, "Because of the need for fiscal restraint, it seems more practical under appropriate circumstances for the County to guarantee the loan rather than actually providing the loan or grant" to the recipient organization. You have asked if a loan guarantee is an acceptable form of financial assistance under Chapter 23B (Chapter 23B loan).

If the County guarantees a Chapter 23B loan, the County would be incurring debt; the fact that the County need only pay the debt if the non-profit organization defaults on its loan does not make the guarantee any less of a debt.

Article 25A, Section 5(P), of the Annotated Code of Maryland authorizes charter counties to borrow money on "the faith and credit of the county" for purposes and on terms as may be provided by local law. Section 5(P) further provides that the authority of the County to borrow money is "subject to any limitations imposed by the charter adopted by the county".

A review of the County Code, most specifically Chapter 20, Finance, reveals no local law authorizing the County to guarantee a Chapter 23B loan. Accordingly, legislation authorizing the County to guarantee a Chapter 23B loan would need to be adopted in order to satisfy the requirement of Article 25A, Section 5(P).

More importantly, however, is the debt limitation provisions of the Charter. Charter Section 312 states, "The County may incur debt. No

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indebtedness for a term of more than one year shall be incurred by the County to meet current operating expenses."¹

The term "operating expenses" is generally understood to mean the normal cost of maintaining and operating County programs. Operating expenses usually involve the costs associated with physical maintenance, administration, salaries, claims, insurance, and rentals. The concept of "operating expense" is more clearly understood when viewed in relation to the concept of "capital expense". A capital expense is an expenditure to acquire property or make a substantial improvement to property. Examples of a capital expense include buying a park, building a road, replacing a roof. See, County Attorney Opinion No. 74.048.

In my opinion, guaranteeing a Chapter 23B loan would be considered as an operating expense rather than a capital expense. Accordingly, the County could not guarantee a loan for a term that exceeds one year. This limitation would, as a practical matter, create a severe limitation on the ability of the County to guarantee a loan since most loans would presumably be for a term in excess of one year.

Finally, I note that your memorandum implies that guaranteeing a Chapter 23B loan would be an advantage to the County because it would not involve a direct outlay of public funds. This advantage, I believe, may be illusory because the County would have to encumber funds sufficient to cover the liability. Accordingly, these funds would not be available for use by the County to meet other expenses. Even if the guarantee could be treated as a capital expenditure (as opposed to an operating expense) a loan guarantee would reduce the County's borrowing authority for other projects.

I trust you will find this memorandum responsive to your inquiry. If you have further questions, please do not hesitate to contact me at X7761.

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cc: William H. Hussmann, Chief Administrative Officer
Ernie Wormwood, Department of Family Resources

¹Charter Section 312 was amended in November 1990 to eliminate the requirement that indebtedness be issued "on a serial maturity plan providing for the maturity of the series in consecutive annual installments, no one of which shall be less than 50% of the amount of any other installment of the series". This provision, as a practical matter, would have prevented the County from guaranteeing most commercial loans that a non-profit organization could obtain, because such loans are not made on a serial maturity plan. This provision, in part, was the basis for the doubts expressed to Ernie Wormwood that were noted in your memorandum.