



NATIONAL CREDIT UNION ADMINISTRATION
Washington, D.C. 20456

December 1, 1986

Office of General Counsel

GC/JT:sg
4630

Mr. John U. Barker
Manager
Hudson River Teachers Federal Credit Union
2085 E. Main Street (Rt. #6)
Peekskill, New York 10566

Dear Mr. Barker:

This is in response to your letter of October 8, 1986, concerning the right of a Federal credit union (FCU) to offset a member's shares against the outstanding balance on his defaulted loan.

It is important to point out that an FCU cannot offset a member's shares against a defaulted debt to the FCU. The legal concept of offset involves the mutuality of obligations which is not present here. However, an FCU can avail itself of the statutory lien authorized by the Federal Credit Union Act.

Section 107(11) of the Federal Credit Union Act (12 U.S.C. §1757(11)) states that a Federal credit union "shall have the power . . . to impress and enforce a lien upon the shares and dividends of any member to the extent of any loan made to him and any dues or charges payable by him." See also Interpretative Ruling and Policy Statement (IRPS) 82-5, a copy of which is enclosed.

Section 107(11) empowers an FCU to impress a lien against shares held by the member at the time the loan is made, as well as against all subsequently acquired shares, to the extent of the unpaid loan balance together with interest, fees, and other charges. The lien may be enforced by applying these shares against the outstanding indebtedness. It is suggested that you refer to IRPS 82-5 for a discussion with respect to when a lien is impressed.

With your letter you enclosed a document which is used by the FCU as its Note. The same document also includes a pledge of shares agreement. You asked whether the FCU would be limited to the shares specifically pledged as collateral or could the FCU still avail itself of its statutory lien (you referred to it as offset). Provided the FCU has properly impressed its lien (as

(FOIA) Vol III Part C #110 Set-Offs

Mr. John U. Baker

Page Two

discussed in IRPS 82-5), it would not be limited to the shares specifically pledged. It should be understood that the statutory lien is something different than a consensual lien (a security agreement) and operates independent of any rights afforded the FCU pursuant to a security agreement with the member.

Additionally, your letter appears to draw a distinction between the maker and the co-maker and asks whether the FCU would somehow be limited as to its right to proceed against the co-maker's shares. The maker and co-maker are jointly and severally liable. What this means is that the FCU is free to go against both the maker and co-maker or either individually. To the extent that each is liable, his/her shares would be subject to the FCU's statutory lien, assuming that the FCU has taken appropriate steps to impress and enforce the lien.

Lastly, during our review of your Note and Pledge document, we discerned what appears to be an inconsistency in that the note states that all shares are pledged as security for the loan while the final part of the document, "Pledge of Shares," permits the member to pledge only a portion of his shares. You may want to have your attorney review this document.

I hope that we have been of assistance.

Sincerely,



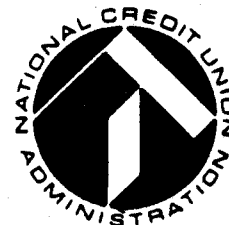
STEVEN R. BISKER
Assistant General Counsel

JT:sg

Enclosure

NATIONAL CREDIT UNION ADMINISTRATION

**INTERPRETIVE RULING
AND POLICY STATEMENT**



IRPS 82-5

DATE: December 22, 1982

NATIONAL CREDIT UNION ADMINISTRATION

12 C.F.R. Part 701

Statutory Lien;

Final Interpretive Ruling and Policy Statement

Enclosure

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final Interpretive Ruling and Policy Statement.

SUMMARY: Even if a member's loan is not secured by shares, under the Federal Credit Union Act a Federal credit union has the power to impress and enforce a lien upon that member's shares and dividends. NCUA is interpreting the Federal Credit Union Act to authorize a Federal credit union: (a) to impress a lien at the time the loan is granted, for instance, by noting the existence of the lien in its records at the same time the loan is granted, by reciting in the loan documents that shares and dividends are subject to the lien or are pledged to secure the loan, or by adopting a bylaw or board policy to the same effect; and (b) to enforce the lien by applying the shares and dividends directly to the amount due on the loan without obtaining a court judgment, even if the credit union has allowed the member to make withdrawals and even if a court judgment would be required under state law before a statutory lien could be enforced.

EFFECTIVE DATE: December 16, 1982.

FOR FURTHER INFORMATION CONTACT: Robert M. Fenner, Deputy General Counsel, or John L. Culhane, Jr., Senior Attorney, Department of Legal Services, National Credit Union Administration, 1776 G Street, N.W., Washington, D.C. 20456 or telephone: (202) 357-1030.

SUPPLEMENTARY INFORMATION: Section 107(11) of the Federal Credit Union Act states that a Federal credit union "shall have the power . . . to impress and enforce a lien upon the shares and dividends of any member to the extent of any loan made to him and any dues or charges payable by him." 12 U.S.C. 1757(11). Since 1979, NCUA had taken the position that before a Federal credit union could enforce this lien it had to obtain a court judgment on the debt, unless state law would allow the credit union to enforce the lien without going to court; once the credit union were to obtain a court judgment, it could then apply the member's shares to the outstanding loan balance. Credit Manual for Federal Credit Unions 29 (Dec. 1979 ed.).

A credit union trade association and an attorney who represented several credit unions asked NCUA to reconsider this interpretation, noting that it placed a credit union at a disadvantage with respect to any other financial institution, which can usually offset a borrower's loan without going to court. After examining the legislative history of and prior administrative interpretations of the statute, NCUA proposed to interpret section 107(11) of the Federal Credit Union Act to preempt state law and to authorize a credit union to enforce the lien on the shares and dividends of a member by applying those shares and dividends to the outstanding loan balance, as that interpretation appeared to be more consistent with Congressional intent and with the contemporaneous administrative interpretations of the statutory language. 47 Fed. Reg. 44340 (1982).

Comments on the proposed interpretation were submitted by 31 credit unions, 4 state credit union leagues, 2 national credit union trade associations, and 3 attorneys (two of the attorneys represent state credit union leagues, the other attorney represents a number of credit unions). The commentors unanimously supported NCUA's proposed interpretation, although one of the attorneys and one of the trade associations requested that rather than limiting the interpretation to enforcement of the lien in the event of default, NCUA expand the interpretation to discuss when the lien may be impressed and to discuss the consequences of permitting withdrawals. The NCUA Board concurs with these commentors that it would be best to address these related issues in one interpretive ruling and policy statement.

Based on an examination of the legislative history and the contemporaneous administrative interpretations of the statutory language, NCUA believes that Congress intended for the statutory lien to be a "floating" lien. That is, a Federal credit union that has impressed a lien on a member's accounts possesses a lien on those accounts at any time to the extent of the unpaid loan balance together with interest, fees, and other charges. The lien "floats" as outstanding obligations, as well as account balances, vary from time to time. The lien enables a credit union to take priority over other creditors when claims are asserted against a member's accounts. See D. Bridewell, Bridewell on Credit Unions 710 (1942 ed.) (quoting from the May-June, 1940 edition of Cooperative Savings, an official publication of the Farm Credit Administration, the agency then charged with administering the Federal Credit Union Act).

If the credit union evidences its intent to do so, it may impress the lien when the loan is granted. This may be done, for instance, by noting the existence of the lien in the credit union's records at the same time the loan is granted, by reciting in the loan documents that shares and dividends are subject to the lien or are pledged to secure the loan, or by adopting a bylaw or board policy to the same effect. See Credit Manual for Federal Credit Unions 16, 17 (May 1972 ed.); Handbook for Federal Credit Unions 18 (July 1947 ed.). Further, even though the lien has been impressed, the credit union may permit routine withdrawals from a member's account without waiving the statutory lien, even if the withdrawals would reduce the account balance to a level below the outstanding indebtedness.

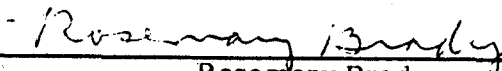
Generally, a credit union may enforce the lien on the shares and dividends of the member by applying those shares to the outstanding indebtedness. Section 107(11) of the Federal Credit Union Act preempts state law; the credit union does not have to obtain a court judgment to enforce the lien, even if a court judgment is usually required under state law before a statutory lien can be enforced. However, if the outstanding indebtedness is the result of extensions of credit under a credit card program, Section 169 of the Truth in Lending Act, 15 U.S.C. 1666h, and Section 226.12(d) of Regulation Z, 12 C.F.R. 226.12(d), will apply; these provisions generally prohibit a Federal credit union from offsetting a borrower's indebtedness arising from a consumer credit transaction under a credit card plan against funds held by the credit union.

Accordingly, the NCUA Board is adopting a final interpretive ruling and policy statement to read as follows.

Interpretive Ruling and Policy Statement (IRPS) 82-5

Section 107(11) of the Federal Credit Union Act states that a Federal credit union "shall have the power . . . to impress and enforce a lien upon the shares and dividends of any member, to the extent of any loan made to him and any dues or charges payable by him." If a credit union evidences its intent to do so, it may impress the lien when the loan is granted. This may be done, for instance, by noting the existence of the lien in the credit union's records at the same time the loan is granted, by reciting in the loan documents that shares and dividends are subject to the lien or are pledged to secure the loan, or by adopting a bylaw or board policy to the same effect. The lien dates from the time it is impressed and applies to all of the member's shares outstanding at the time the loan is made. If during the loan term the member's shares are reduced by withdrawal or increased by deposit or dividend payments, the lien will apply to the balance of the same from time to time and may be enforced with respect to any shares in existence at the time of enforcement. The credit union may enforce the lien on the shares and dividends of the member by applying those funds directly to the outstanding indebtedness, which may include the unpaid loan balance together with interest, fees, and other charges. The credit union does not need to obtain a court judgment to enforce the lien, even if a court judgment is usually required under state law before a lien can be enforced.

By the National Credit Union Administration Board, December 16, 1982.



Rosemary Brady
Secretary
National Credit Union Administration Board