



NATIONAL CREDIT UNION ADMINISTRATION  
Washington, D.C. 20456

September 5, 1989

Office of General Counsel

GC/MM:sg  
SSIC 8001  
89-0731

Ms. Sarah B. Cummer  
Credit Union National Association, Inc.  
805 15th Street, N.W.  
Suite 300  
Washington, D.C. 20005-2207

Re: Payroll Deduction/Termination of Member  
Accounts (Your July 26, 1989, Letter)

Dear Ms. Cummer:

You have asked the following questions: (1) Is it permissible for a Federal credit union ("FCU") to establish a written policy that loans repaid to the credit union by payroll deduction can be made at rates below identical loans that are not repaid through a payroll deduction system? Yes. (2) If a member defaults on a loan to the FCU and the FCU properly withdraws all funds in the account to apply to the outstanding loan balance, is the person's membership terminated? No. Is Article III, Section 3 of the Standard Bylaws applicable to this situation? Yes. Does the member have to be notified that he has a certain time to raise his account to one share? Yes, members should be notified of the policy. (3) If a member's account is reduced to zero by an outside third party, is the person's membership terminated? No.

ANALYSIS

(1) You have asked whether it is permissible for an FCU to establish a written policy that loans repaid to the FCU by

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payroll deduction can be made at rates below identical loans that are not repaid through a payroll deduction system. An FCU board of directors may set interest rates on loans as long as they comply with the guidelines of Section 107(5) of the FCU Act (12 U.S.C. §1757(5)). This section of the FCU Act is silent on interest rate differentiation. Section 701.21 of the NCUA Rules and Regulations (12 C.F.R. 701.21) controls loans to members. Written loan policies are discussed in Section 701.21(c)(2) which provides:

(2) Written policies. The board of directors of each Federal credit union shall establish written policies for loans and lines of credit consistent with the relevant provisions of the Act, NCUA's regulations, and other applicable laws and regulations.

The allowable interest rate on loans is provided for in Section 701.21(c)(7)(i). It states:

(i) General. Except when a higher maximum rate is provided for in 701.21(c)(7)(ii), a Federal credit union may extend credit to its members at rates not to exceed 15 percent per year on the unpaid balance inclusive of all finance charges. . . .

Section 701.21(c)(7)(ii) currently permits rates of up to 18 percent per year.

There is nothing in the FCU Act or NCUA Rules and Regulations prohibiting an FCU from establishing a written policy that loans repaid to the FCU by payroll deduction can be made at rates below identical loans that are not repaid through a payroll deduction system.

(2) You have asked whether a person's membership in an FCU is terminated if the FCU properly withdraws all funds in the account to apply to an outstanding loan balance. As a corollary to this, you have also asked whether Article III, Section 3 of the Standard Federal Credit Union Bylaws (FCU Bylaws) applies to this situation and also whether there is any notification requirement to the member. Article III, Section 3 of the FCU Bylaws provides:

Section 3. A member who fails to complete payment of one share within \_\_\_\_\_ of his admission to membership or within \_\_\_\_\_ from the increase in the par value of shares, or a member who reduces his share balance below the par value of one share and does not

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increase the balance to at least the par value of one share within \_\_\_\_\_ of the reduction may be terminated from membership. (Note: The board shall specify the time period of at least 6 months and insert the same time periods in each blank.)

Article III, Section 3 has been interpreted to apply when a member's account falls below the equivalent of a single share or when it is involuntarily reduced by the FCU through the assessment of maintenance fees, late charges, or statutory lien. Therefore, in your situation, the member's account would not be terminated for a period of at least six months after the application of the statutory lien. In Letter to Credit Unions No. 70, dated November 29, 1982, notification to a member was discussed in relation to a possible loss of membership due to the application of Article III, Section 3. It states:

Since this standard bylaw amendment may result in loss of membership if payment of one share is not fully completed within the specified time frame, Federal credit unions adopting the amendment should notify all members of the change and what they must do to avoid adverse consequences.

We have not taken the position that notification to a member is necessary each time a share account is reduced below par value. However, members should be aware of the FCU's policy of closing an account based on its falling below par value due to absorption through lien or fees.

In your scenario, Article III, Section 3 is triggered when the member's account is reduced to below par value or to zero. As noted above, we have interpreted Article III, Section 3 to apply when par value is reduced due to the FCU's statutory lien. A member must be given at least six months to bring his/her account back up to par.

(3) You have also asked whether a person's membership is terminated if the member's account is reduced to zero by an outside third party. The analysis here is the same as in (2) above. Therefore, Article III, Section 3 of the Standard

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Bylaws is applicable and the member's account would not be terminated for a period of at least six months after the account is reduced to zero.

Sincerely,

*Hattie M. Ulan*

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Assistant General Counsel