

April 3, 1997

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Re: Ability of FCUs to Make First Lien Home Improvement Loans in Texas
(Your November 26, 1996, Letter)

Dear Mr. Martin:

You have asked whether Section 701.21 of NCUA's Rules and Regulations, 12 C.F.R. §701.21, preempts a provision of the Texas Consumer Credit Code which prohibits home improvement loans secured by first liens. NCUA's regulation preempts the Texas statute.

The statute provides that:

No retail installment contract or retail charge agreement shall:

....

(7) Provide for or grant a first lien upon real estate to secure such obligation, except, (a) such lien as is created by law upon the recording of an abstract of judgment or (b) such lien as is provided for or granted by a contract or series of contracts for the sale or construction and sale of a structure to be used as a residence so long as the time price differential does not exceed an annual percentage rate permitted under either this Chapter or Article 1.04 of this Title.

TEX. REV. CIV. STAT. art. 5069-6.05(7) (West 1987). Your letter notes that the above-quoted provision has been held to prohibit home improvement loans secured by a first lien. *Ibarra v. Diversified Services*, 894 S.W.2d 1 (Tex.App.--Amarillo 1994).

Section 701.21(b)(1)(iii)(B) and (C) of NCUA's Regulations provide that state law is preempted with respect to "the purpose of the loan or line of credit" and "the type or amount of security and the relation of the value of the security to the amount of the loan or line of credit." A state statute prohibiting home improvement loans secured by first liens falls within the area of lending the NCUA Board has determined is preempted by federal law and is, therefore, not enforceable against federal credit unions. Home improvement is the purpose of the loan and the securing of a loan by a first lien is a condition related to the type of security.

In order to avoid any potential confusion, we note that section 701.21(b)(2), which lists matters not preempted by federal law, includes "laws related to transfer of and security interests in real and personal property." 12 C.F.R. §701.21(b)(2)(ii). This section is intended to apply only to state laws governing the recording and transfer of security interests and not the type of security.

I hope that we have been of assistance.

Sincerely,

Sheila A. Albin
Acting Associate General Counsel

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cc: Region V, Regional Director