July 28, 2004

Mr. Rodney Dauteuil
28 Pleasant View Street
Methuen, MA 01844-3945

Re: Overdrawing an Account to Enforce a Statutory Lien.

Dear Mr. Dauteuil:

You have asked if the statutory lien provision in §107(11) of the Federal Credit Union Act (the Act) permits a federal credit union (FCU) to overdraw a member's regular share or share draft account to credit the member's overdue loan payment. 12 U.S.C. §1757(11). The Act and NCUA regulations do not permit an FCU to overdraw an account. An FCU may only create an overdraft if there is an agreement between the member and the FCU to that effect.

You describe a situation where a member's loan becomes past due and the FCU transfers the full amount of the payment due from the member's regular share or share draft account to the loan despite the fact that the member's account does not contain sufficient funds to cover the full payment. NCUA regulations define a statutory lien as "a right in or claim to a member's shares and dividends equal to the amount of that member's outstanding financial obligations to the credit union, as that amount varies from time to time." 12 C.F.R. §701.39(a)(5). We think it clear from this language that an FCU may only impress the statutory lien on the existing balance in a member's accounts, including dividends, and cannot use the statutory lien authority to create an overdraft or overdraw an account

You also indicate that the FCU has two overdraft products that are available only on share draft accounts; an overdraft protection plan and an overdraft line of credit. If the member has one of these plans and the underlying loan agreement expressly permits the FCU to trigger the overdraft coverage on a share draft account in the event of a past due payment, then the FCU may do so in accordance with the terms of the loan agreement. We note below that we question if there is any real benefit to the member or the FCU with this approach and may, in fact, be confusing to the member and delay collection of an overdue loan payment.

Finally, you ask if an overdraft to make a loan payment would constitute a loan itself and be subject to all the requirements in our general lending rule. 12 C.F.R. §701.21. Overdrafts are specifically addressed in §701.21(c)(3). Under the provisions of that section, an FCU must have a written overdraft policy in place in order to pay an overdraft. The written policy must address all the requirements of that section including establishing "a time limit not to exceed forty-five calendar days for a member either to deposit funds or obtain an approved loan from the credit union to cover each overdraft." Id. The situation you describe would create a debt to the FCU that the member must pay within the terms of the overdraft policy or the member must obtain a loan meeting the requirements of the general lending rule. While this mechanism may provide some benefit to a member, in essence, an additional period of time for a member to make a loan payment, we think it presents some risks. You note that, when the credit union overdraws a share draft account to make a loan payment, it does not assess an overdraft charge. This approach could create confusion about whether any additional fees and interest are being assessed under the terms of the loan or as part of an overdraft product. We also question whether this approach results in delaying the recording of an overdue loan and suggest you consult with the appropriate NCUA regional office as to any safety and soundness concerns it may have with using an overdraft plan in this manner.

Sincerely,

/S/

Sheila A. Albin
Associate General Counsel

OGC/DMS/SAA:bhs
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