

Department of Legislative Services
Maryland General Assembly
2017 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 568
Economic Matters

(Delegate Shoemaker)

Financial Institutions - Credit Unions - Liens and Rights to a Setoff

This bill establishes that a credit union does not have a lien or a right to a setoff if a member of the credit union has filed for bankruptcy. Under the bill, if a credit union member files for bankruptcy and is delinquent or in default either on a loan from the credit union or any dues, charges, fees, fines, or other amount payable to the credit union, then the credit union may not immediately apply the value of shares or deposits of the member who has filed for bankruptcy to defray the loss.

Fiscal Summary

State Effect: None. The bill pertains exclusively to private-sector activities.

Local Effect: None.

Small Business Effect: Potential meaningful.

Analysis

Current Law: Under § 6-314 of the Financial Institutions Article, if a credit union member is delinquent or in default on (1) any outstanding loan (whether or not matured) on which the member is liable to the credit union or (2) any dues, charges, fees, fines, or other amount payable to the credit union, then the credit union has a lien and a right to a setoff on the shares and deposits of that member (including any dividends or interest payable on those shares or deposits). The lien and right to setoff conferred by State law exists without the credit union being required to take any action to perfect the lien.

If a member resigns or is expelled, a credit union may cancel a member's shares and apply his or her withdrawal value against any amount owed to the credit union by the member. The credit union may allow a member to withdraw shares or deposits without affecting its lien or right to a setoff. A credit union may also refuse to allow a member to withdraw shares or deposits to the extent of any delinquency or default.

Background: The Office of the Commissioner of Financial Regulation of the Department of Labor, Licensing, and Regulation is responsible for chartering, supervising, and regulating Maryland State-chartered credit unions. According to the Office of the Commissioner, there are eight State-chartered credit unions in Maryland. National or federally chartered credit unions are regulated by the National Credit Union Administration and insured by the National Credit Union Share Insurance Fund, which is backed by the full faith and credit of the U.S. government. Federally chartered credit unions generally have the word "federal" in their names.

The commissioner advises that § 6-314 of the Financial Institutions Article authorizes State-chartered credit unions to have a lien against members that has priority over all other creditors. To the extent that a credit union member is in default on any loan owed to the credit union, then, pursuant to its lien, the credit union can "set off," or reduce, the amount the member owes by the amount the credit union owes to the member on account of the member's share and deposit accounts.

Federal bankruptcy code (11 USC § 553) explicitly recognizes the credit union's lien and right of setoff. Further, federal bankruptcy law treats the State-chartered credit union's lien and right to a setoff as a secured claim. By removing the lien and the credit union's right to setoff in the event of a member's bankruptcy, a State-chartered credit union's claim becomes unsecured. The commissioner further advises that unsecured claims are only paid if there are funds available after payment of all bankruptcy administrative expenses and secured creditors' claims. Thus, unsecured claims are typically not repaid in full.

Small Business Effect: To the extent that any of Maryland's State-chartered credit unions are small businesses, the bill potentially impacts them significantly. Under State law, if a credit union member has a loan with the credit union and files for bankruptcy, the credit union has a lien (*i.e.*, a claim) and a right to a setoff. Because the credit union is given priority over other creditors (*i.e.*, creditors without a lien), it is more likely to receive the amount that it is owed than the creditors who have a lower lien priority or those creditors without a lien.

Under the bill, credit unions that have outstanding loans to members who file for bankruptcy may be less likely to recoup the losses resulting from loans made to such members. The change could significantly impact a credit union's ability and willingness to lend to its members. However, any impact depends on the extent to which

State-chartered credit unions have members with outstanding loans or debts owed to them who also file for bankruptcy.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Judiciary (Administrative Office of the Courts); Department of Labor, Licensing, and Regulation; Office of the Comptroller of the Currency; U.S. Department of the Treasury; mycreditunion.gov; Department of Legislative Services

Fiscal Note History: First Reader - February 14, 2017
fn/kdm

Analysis by: Eric Pierce

Direct Inquiries to:
(410) 946-5510
(301) 970-5510