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May 1, 2007

Mary Rupp, Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314-3428

**Re: Umholtz Comments on Proposed Rule 701.3, Member Inspection of Credit Union Books, Records, and Minutes**

Dear Ms. Rupp:

I appreciate having the opportunity to present my comments to the Members of the NCUA Board concerning Proposed Rule 701.3 regarding Member Inspection of Credit Union Books, Records, and Minutes. My comments are intended to be candid and, where critical of NCUA, are not intended to be disrespectful. If you have any questions concerning these comments, please feel free to contact me for clarification or elaboration.

**Proposed Rule and Accompanying Assumptions Are Bad Public Policy**
NCUA Proposed Regulation 701.3 concerning Member Inspection of Credit Union Books, Records and Minutes is bad public policy. The NCUA summarizes the rule's impact as, "The rule provides that a group of members representing approximately one percent of the membership, with a proper purpose and upon petition, may inspect and copy the nonconfidential portions of the credit union's books, records, and minutes."

This proposed rule and NCUA's continuing interpretations about credit union member rights greatly favor dissident groups and outside agitators that seek to disrupt a credit union's governance and decision-making process. It appears that NCUA is attempting to end-run recent judicial decisions that said that credit union members more resemble bank depositors than shareholders in a stock company.

The proposed rule positions the NCUA regional directors as referees to determine if the purpose of the dissident-demanded access is legitimate and not just for harassment purposes. Inserting the NCUA regional directors into disputes between the credit union and the dissidents raises concerns about their impartiality, dispute resolution expertise, and ability to render a decision that won't end up in court anyway. A judge is much more likely than a regional director to be impartial and fair.

When credit union members are allowed to cash out their share of the credit union's equity and take it with them to deposit in another financial institution down the street,

then members will truly resemble stockholders. Until that becomes reality, a credit union member is merely a customer with a few voting privileges. NCUA's assumption as illustrated in this proposed rule that a credit union member has the same rights as a stockholder in a for-profit company is erroneous, bad public policy, and sure to be litigated and overturned in court.

**Credit Union Member Rights Are Limited**

Please keep in mind that although credit union members have an individual ownership interest in their credit union in the event of a liquidation, their actual day-to-day relationship is more like that of a customer than like an owner of marketable stock. Since they are organized without capital stock, the applicability of laws designed for stock and other for-profit companies may not appropriately address the credit union relationship with its member.

NCUA Board Members should re-read docket number 32858-5-II from the State of Washington Court of Appeals Division II filed 7/25/06. This Washington Appeals Court ruling in the case of Save Columbia CU Committee *et al*, Appellants v. Columbia Community Credit Union *et al*, Respondents confirms that credit union members are more like customers than stockholders. The Court said, "Columbia's members resemble depositors at a bank more than corporate shareholders." The issues addressed by that Court and its rulings are contrary to many provisions of these proposed NCUA conversion rules. The Court's points should be carefully considered before NCUA finalizes this proposed rule. It certainly makes a stronger case for eventual litigation should NCUA proceed as proposed.

**250 Petition Signature Cap Promotes Governance Disruptions**

The 250 cap on the number of petitioners required to gain access to records (rather than an absolute 1%) disadvantages larger credit unions and overly exposes them to ill-intentioned dissidents and socio-political agitators. The cap promotes the tyranny of the miniscule minority, not the rights of the majority. The chaos caused to several larger federal credit unions by the 750-member petition cap in the FCU Bylaws is well established and illustrated how inappropriate low caps can be for large credit unions. Until the NCUA Board fixes the anachronistic FCU Bylaws and stops asserting that low caps like this proposed 250 are somehow noble, then federal credit union governance stability will remain under a constant threat.

If a credit union's customers, including potentially disruptive parties, can demand to review proprietary and strategically sensitive documents, then why not simply make them available to all potential customers, too? Pundits, curmudgeons, and axe grinders should have equal access. After all, as the NCUA Chairman promised in a recent Media Release, "If NCUA rules are found to be inadequate or insufficient to provide member protection, transparency and fairness, the [NCUA] Board will decisively move to address them." What is more fair and transparent then allowing everyone to look?

The federal credit union bylaws already provide a mere handful of motivated members with the ability to hijack the credit union. Please take no additional steps that would

further undermine the governance stability of a federally chartered or federally insured credit union.

**Sincere Members Have Reasonable Alternatives to Become Informed**

If a credit union member sincerely wants to be informed about a merger, conversion or other strategic matter, he or she should be willing to go in to a branch office by himself or herself, sign a confidentiality agreement, and review the documents. The proposed rule would inevitably be used by dissident groups that are on fishing expeditions to prepare for lawsuits. These groups are often funded by outside interests and seek to publicly second-guess, embarrass, or overthrow a credit union's leadership.

The NCUA Board should instead find a way to regulate the inappropriate behavior of and misleading statements from these dissidents who have demonstrated their disregard for the truth and revealed their disruptive intentions. At the very least, these ill-intended disruptors should be required to pay in advance to see and copy these documents. An alternative would be to require them to post a bond.

The proposed rule appears premised upon the belief that a single credit union member's opinion on a merger, conversion, or other strategic tactic is the functional equivalent to the business decision made by a credit union's duly elected leadership who are statutorily authorized to handle the vast majority of the credit union's operations and business affairs. Placing the individual member on the same level as the credit union's governing body is counterproductive if the agency wants its regulated and insured institutions to remain stable and viable.

**Member Access to Credit Union Books, Records, and Minutes Is Ill-advised**

It has been NCUA's longstanding, but flawed, opinion that the internal governance of federal credit unions, to the extent a matter is not addressed in federal statutes, regulations or bylaws, should be determined by reference to the law governing for-profit corporations in the state in which the federal credit union is located. (NCUA OGC Legal Opinion 96-0541 June 14, 1996).

Despite its assertions, NCUA is ill-advised to incorporate this legal opinion into the rules or substitute this proposed rule. The opinion and proposed rule are highly vulnerable to judicial reversal. The proposed rule becomes an invitation to lawsuits by those opposed to the rule and/or who have high stakes in a merger, conversion, or other strategic tactic.

The previously mentioned Washington Appeals Court case points out why credit union members have no claim on the credit union's records and goes on to rule, "The state's extensive regulatory oversight of Columbia, coupled with the fundamental differences between shareholders of a corporation and members in a credit union, compel the conclusion that Columbia's members do not have the right to inspect the organization's books and records…. Thus, the trial court did not err in dismissing Save CU's access to records claim, insofar as that claim related to records other than bylaws or amended bylaws."

**Credit Unions Are Not Equivalent to Stock Companies**

Credit unions are not-for-profit financial institutions organized cooperatively without capital stock. The rules for for-profit institutions in which individuals can have marketable ownership should not apply to credit unions. As mentioned in previous paragraphs, the relationship between a member and the credit union is more like that of a customer and service provider than it is to a shareholder and a for-profit entity. It may be more logical for NCUA to apply consumer protection laws to the issue of access to records rather than to apply state for-profit corporation laws or this proposed rule.

An individual customer should have no absolute right of access to a credit union's books, records, or minutes under any circumstances. A customer should not have access to the credit union board's due diligence records and similar strategically sensitive information.

The net effect of NCUA's propose rule is to encourage dissidents' fishing expeditions designed to unearth potential governance details with which to sue and/or disrupt the credit union by second-guessing the governing board's due diligence. It is bad public policy. NCUA should instead be doing everything it can to facilitate mergers, conversions, and other strategic business decisions made by a credit union's leaders exercising their fiduciary responsibility to act in the best interest of the entire membership.

Your questions concerning these comments and any requests for additional information are welcome.

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Marvin Umholtz is President & CEO of Umholtz Strategic Planning & Consulting Services based in Castle Rock, Colorado south of Denver. He is a 30-year credit union industry veteran who has held many leadership positions with credit union organizations and financial services industry vendors during those years. An accomplished speaker and former association executive, he candidly shares his credit union industry knowledge and insight with public policy makers, financial industry executives, and vendor companies. In collaboration with GRFI/The Frerichs Group www.grfiltd.com, he provides credit unions with merger evaluation and targeting services. Umholtz also helps financial institution boards and CEOs with strategic issues like growth, technology, charter conversions, regulatory compliance, media advocacy and vendor management. Additionally he serves as membership director for the Coalition for Credit Union Charter Options www.ccuco.org.