



Credit Union National Association

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August 20, 2007

Ms. Mary Rupp  
Secretary to the Board  
National Credit Union Administration  
1775 Duke Street  
Alexandria, VA 22314

Re: NCUA's Proposed Rule to Reincorporate the Bylaws and Make Certain Changes to the Bylaws for Federal Credit Unions

Filed via: [regcomments@ncua.gov](mailto:regcomments@ncua.gov)

Dear Ms. Rupp:

This letter addresses the views of the Credit Union National Association on the National Credit Union Administration Board's proposal to reincorporate the FCU Bylaws into the agency's regulations and to make other changes to the federal bylaws. By way of background, CUNA is the largest credit union trade organization in this country, representing approximately 90% of the nation's almost 8,500 state and federal credit unions, which serve 87 million members.

In recognition of the significance of this proposal, our letter was drafted following the thorough and coordinated consideration of a number of key CUNA policymakers, including the CUNA Examination and Supervision Subcommittee, the CUNA Federal Credit Union Subcommittee, the CUNA Governmental Affairs Committee, and the CUNA Executive Committee. A copy of CUNA's Guidelines on the Enforcement of FCU Bylaws, which forms the basis for CUNA's views discussed in this letter, is attached.

### **Summary of CUNA's Views**

CUNA appreciates the efforts of the Board to develop this proposal and to present a well crafted request for comments that invites public input on significant issues relating to the bylaws. However, while CUNA agrees that the Federal Credit Union Act (Act) empowers NCUA to enforce the bylaws, we do not think



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that all bylaws should be subject to NCUA intervention -- as could be the case under the proposal -- since many bylaw provisions address only routine operational issues. On the contrary, the most reasonable interpretation of NCUA's authority is that it should be very carefully delineated to keep bylaw disputes outside of the examination process and to focus only on bylaw disagreements that involve fundamental issues of members' rights or boards' responsibilities. Yet, aspects of the proposal indicate that may not be the case. We are also concerned that the proposal does not give sufficient deference to the ability of each federal credit union to settle bylaw disputes for itself, first, under its own internal procedures before turning to the agency for assistance.

In light of these concerns regarding the reasonable enforcement of the bylaws, we do not support NCUA's proposed amendment to reincorporate the bylaws by reference into its regulations or the proposed changes to the Introduction to the Bylaws to reflect the reincorporation. Rather, as discussed beginning on page six, we recommend an alternative approach that is fully consistent with the FCU Act, as well as with standards of current jurisprudence regarding agency deference, which we believe will achieve NCUA's objectives in a less burdensome manner for credit unions and the agency. CUNA does support, with some recommended modifications, the proposed bylaw amendment directing a credit union's supervisory committee to function as the credit union's board in the event all of the board members are removed or resign simultaneously.

## **Enforcement of FCU Bylaws**

### **Why This Issue is Significant**

Under the Federal Credit Union Act, federal credit unions must incorporate under bylaws developed by NCUA (12 USC 1758). Such bylaws address not only the conduct of the credit union's business affairs, but also, in certain instances, members' rights of democratic control that are fundamental to the unique qualities of credit unions as cooperatively owned financial institutions.

In 2006 in a well-publicized series of events, members of a federal credit union who did not support their credit union board's decision to convert to a thrift, sought to enforce a bylaw of the credit union that permits members to call a special meeting. The dissenting members wished to remove the credit union's board and to replace it with directors who did not support the conversion. When the board of the FCU refused to hold the special meeting, the members turned to the National Credit Union Administration which, under its current policy, felt it could not intervene, leaving the pursuit of judicial remedies as the dissenting members' only options. Regrettably, such options have not yet proven fruitful.

As a result, the very nature of the bylaws has been jeopardized, creating an atmosphere of uncertainty as to whether compliance with bylaws is even

necessary. As discussed below, however, rather than the broad regulation NCUA is proposing, we strongly recommend the agency adopt a more measured approach.

### **NCUA's Views Regarding the Scope of Its Current Authority**

As discussed in the Supplementary Information to the proposal (72 FR 30984), the Federal Credit Union Act unquestionably authorizes the agency to liquidate or remove a credit union's charter for failure to comply with its bylaws (12 USC 1766). However, NCUA has taken the view that the implementation of lesser sanctions, such as intervening in bylaw disputes, could be problematic. When the bylaws were part of the regulations, "NCUA's authority to enforce bylaw violations through less severe administrative remedies ... was clear because such violations could be viewed as a violation of NCUA's regulations, thus enabling NCUA to bring a variety of administrative enforcement actions to effect compliance in appropriate cases," the Supplementary Information states.

Thus, NCUA's decision to remain neutral on bylaw issues was based on the agency's deregulation of the bylaws and its concern over the scope of its present authority. Until 1982, NCUA had incorporated the FCU Bylaws into its regulations through references in three separate provisions of its rules. However, in an effort to deregulate credit union operations consistent with actions taken by other federal financial regulators at the time, the NCUA Board removed two references in its regulations to the bylaws. The third reference was removed in 1999 as a technical change.

NCUA's decision to stay out of the bylaw dispute also reflected its current legal opinions that the agency will not become involved in bylaw issues absent a safety and soundness concern and that bylaw disputes should generally be resolved under state corporate law.

Now, in an effort to reclaim its authority to enforce the bylaws and to "take administrative actions when a credit union is not in compliance with its bylaws," the agency is proposing to reinstate the bylaws in the regulations by reference and to change the Introduction to the Bylaws. NCUA states in the proposed changes to the Introduction that it "will not take action against every minor or technical violation" but nonetheless, "retains discretion to enforce the bylaws in appropriate cases, which may include, **but are not limited to**, safety and soundness concerns or threats to fundamental material credit union members' rights." (72 FR 30988)

### **CUNA's Concerns with NCUA's Approach**

Four new proposals from NCUA this summer, including this one on the bylaws, plus examiner demands under the Bank Secrecy Act, have caused some credit

unions to question whether and why the agency is adopting a more proactive regulatory posture.

CUNA does not believe that the agency's objective is to micromanage credit unions through the bylaws. However, there are several aspects of the proposal that sanction open-ended enforcement authority that we cannot support.

As proposed, NCUA would move its position on bylaw enforcement from virtually no involvement to one that claims broad authority to enforce a bylaw that it deems is "an appropriate case." More to the point, even though the Supplementary Information to the proposal says NCUA will focus on bylaws that address members' rights, the proposal would reincorporate by reference **all** of the bylaws, giving the agency the authority to enforce any and every bylaw -- even those that are ministerial in nature and do not address issues of members' rights.

The proposal contains several indications that the agency is seeking substantial new authority, despite the assurances of the Supplementary Information to the contrary (72 FR 30986). For example, one of the citations to the Act that the agency provides as authority for the proposal is 12 USC 1756, which addresses the agency's power to supervise and examine federal credit unions. Settling bylaw disputes should not be the purview of examiners.

The Supplementary Information states, "NCUA also believes it should have the ability to institute an enforcement action when a bylaw violation poses a threat to fundamental, material credit union member rights" (72 FR 30986). However, by incorporating the bylaws into the regulations, such enforcement actions could take many forms as NCUA has the authority to impose a number of sanctions for regulatory violations, including citations in an exam report, lowering CAMEL ratings or prompt corrective action categories and assessing fines.

We also have concerns that NCUA would *initiate* action to resolve bylaw disputes when we believe the proper role of the agency in this context is to respond to a request from credit union parties for assistance.

In short, NCUA's approach to reincorporate the bylaws by reference, as described in the Supplementary Information, is too undefined and inclusive. We are particularly concerned since there is nothing in the actual language of the proposed rule or new Introduction that limits the application of the agency's sanctions, precludes examiner involvement, or that indicates the agency would wait until asked by credit union parties to resolve a dispute.

Further, we believe it is not necessary for NCUA to adopt a new rule in order to be able to respond to bylaw disputes. The most reasonable reading of the Act is that NCUA has authority to address bylaw disputes through actions that are short of liquidating a credit union or removing its charter. If, in fact, the statute only permits bylaw issues to be addressed through liquidation or charter removal, then no regulation from NCUA that purports to permit lesser sanctions will fill the regulatory gap and allow the agency to create such authority.

Our conclusion that NCUA currently has authority to help settle bylaw disputes, such as the one presented in the DFCU situation, is based on several provisions in the Act. First, the Act requires NCUA to develop model bylaws, which “shall be used” by FCU incorporators and the proposed credit union’s bylaws must be submitted for agency approval (12 USC 1758). The Act also requires that “special meetings may be held in the manner indicated in the bylaws” (12 USC 1760) and includes a number of other provisions that require a federal credit union to act in a fashion that is consistent with its bylaws (12 USC 1761; 1761a; 1761b; 1761c. Such provisions address the duties of the board and committees and other issues such as compensation of officers, which all must be in accordance with the federal credit union’s bylaws.)

Further, the Act states that NCUA “may” liquidate or revoke a credit union’s charter for bylaw violations, not that it “must” take such action. This language supports the appropriate conclusion that NCUA is empowered to use its discretion in several ways: to liquidate or not; revoke a charter or not; or help settle bylaw disputes of the kind represented in the DFCU situation without resorting to the most draconian sanctions, which represent the outer limits of NCUA’s permissible authority.

Taken together, these measures strongly indicate that a federal credit union may be expected to act in accordance with its bylaws. Just as important, these provisions also indicate that NCUA, as the administrator of the Act and its statutory directives to federal credit unions, has an appropriate role to ensure bylaws are upheld when disputes arise. These provisions further underscore that no new rule to require such action on the part of credit unions or NCUA is needed, because the Act already provides ample authority for NCUA to handle these matters.

We also do not believe that a regulation is necessary in order for the courts to afford NCUA deference, should future bylaw disputes be the subject of litigation.<sup>1</sup>

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<sup>1</sup> In the most recent bylaw case in the U.S. District Court for the Eastern District of Michigan, Southern Division (*Sly et al v. DFCU Financial Federal Credit Union*, 7/26/06), the judge stated in dicta that the court could not provide a federal remedy for breach of the bylaws as NCUA had “declined to give the federal credit union bylaws the weight of an agency regulation and stated that enforcement of

We base this conclusion in part on Supreme Court decisions that have indicated federal courts may give deference to agency actions that do not involve regulations. (See for example, *National Cable & Telecommunications Assn. V. Brand X Internet Services*, 345 F. 3d 1120, 2005)

Congress has given NCUA considerable authority to implement the Act, either through regulations or other policies and interpretations, as other agencies with similar functions are permitted to exercise. Under this authority, NCUA has conducted a notice and comment process, signaling to the public that it is considering a policy change on bylaw enforcement. If after that process is concluded the agency determines it should change its policy regarding the enforcement of the bylaws, whether through a rule or by solely amending the Introduction as CUNA is recommending, the agency's action is entitled to deference under the Administrative Procedure Act if it is not arbitrary or capricious and is consistent with the Act. (*U.S. v. Mead Corp.*, 533 U.S. 218 (2001)), holding an agency order was not due deference but recognizing agency actions that are not rules may be afforded deference; *Medtronic, Inc. v. Lohr*, 518 U.S. 470 (1996); *National Cable & Telecommunications Assn.*, 345 F. 3d 1120, Justice Breyer concurring).

Further, in our view, NCUA's proposed policy change regarding bylaw enforcement is in the nature of preemption in that federal credit unions could have a remedy from NCUA that would preclude their need to invoke state corporate law in state litigation. We believe such a preemption policy developed under a notice and comment process would have deference whether it results in a rule or some other policy action. ( See for example, Justice Breyer's concurring opinion in *Medtronic* at 505: "In the absence of a clear Congressional command as to preemption, courts may infer that the relevant administrative agency possesses a degree of leeway to determine which rules, regulations or other administrative actions have preemptive effect.")

### **CUNA's Alternative**

Instead of incorporating all of the bylaws into the rules, we think the agency's goals would be better accomplished in a simpler, less intrusive yet as effective

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the bylaws is generally undertaken pursuant to state corporate law." The opinion is not a treatise on agency deference but rather addresses how the particular dissenting member plaintiffs could have obtained jurisdiction in federal district court in that case. It was appropriate for the court to summarize the jurisdictional issues as it did. NCUA previously treated the bylaws as a regulation but no longer does, and has issued several legal opinions directing potential bylaw litigants to state court. In essence, the Court deferred to NCUA's current policy determination that bylaw disputes are a matter for state law to resolve.

manner by amending the Introduction to the Bylaws. This action would provide sufficient notice to stakeholders that the agency has changed its policy on bylaw enforcement and will be available to help resolve bylaw disputes that cannot be settled through a credit union's internal process.

In that connection, we propose that paragraph six of the Introduction to the FCU Bylaws be revised to state:

Federal credit unions are expected to comply with their bylaws, consistent with the Federal Credit Union Act. The bylaws function as a contract between the members and the credit union and also address provisions required by federal law. In addition, the bylaws help define credit union board members' fiduciary duties and the rights of members to participate in the affairs of the credit union.

On rare occasions, bylaw disputes may arise as to whether a federal credit union is complying with a bylaw as it relates to members' fundamental rights. Such bylaws include members' rights to call and attend special meetings; petition for the removal of directors and committee members with due cause; participate in the election of directors; and maintain federal credit membership.

Federal credit unions are encouraged to first settle such disputes under an internal process involving the supervisory committee or other appropriate internal body, as determined by the credit union.

If such a process does not first resolve the dispute, federal credit union parties may request their NCUA regional director to help settle the disagreement. Regional directors will be expected to work with the credit union and its members to resolve the issues cooperatively and in a reasonable time frame. Such bylaw disputes will never be addressed in the federal examination process nor will the agency become involved in bylaw disputes involving issues that are strictly operational or ministerial.

Consistent with the Federal Credit Union Act and the agency's longstanding policy, NCUA may also enforce bylaws based on material safety and soundness concerns, if the need arises.

### **What is Gained By Avoiding a New Rule**

While we believe the matter of bylaw enforcement is a very important one, incorporating the entire bylaws by reference into the regulations, thereby facilitating agency intrusion into the operations of credit unions on even the most mundane operational issues, is too imprecise a remedy for the current ills associated with enforcement. By avoiding such action and instead carefully

addressing the agency's policy and intent toward enforcement in the Introduction to the Bylaws, NCUA properly effects policy changes without subjecting credit unions to the specter of unwarranted intrusion from examiners. We feel this would be a significant accomplishment.

### **If NCUA Determines a Rule Is Necessary**

If NCUA determines that it must also adopt a regulation, then we recommend the Board amend 12 CFR 701.2(a) and (b) of the proposal as follows, retain sections 'c' and 'd' as proposed, as well as adopt the proposed changes to the Introduction to the Bylaws that CUNA is proposing above:

The Federal Credit Union Act requires federal credit unions to develop and maintain bylaws that are consistent with the Act. A copy of the Federal Credit Union Bylaws may be obtained at <http://www.ncua.gov> or by request addressed to the National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314.

In the rare instance that a bylaw addressing members rights is the subject of a dispute between a credit union's board and membership that cannot be resolved under the credit union's internal process, the credit union's NCUA Regional Director may be requested by the interested parties to help settle the dispute, consistent with the Introduction to the Federal Credit Union Bylaws.

### **New Standard Bylaw on the Duty of the Supervisory Committee to Act on the CU Board when the Board has been Removed**

NCUA is also proposing that a new standard bylaw be adopted that directs the supervisory committee to assume the credit union board's functions should all members of the board be simultaneously removed or resign from their offices. We support this amendment with some suggested changes to facilitate its operation.

Proposed Section 3 of Article IX: If all director positions become vacant simultaneously, the supervisory committee immediately assumes the role of the board of directors and must generally call and hold a special meeting to elect a board that will serve until the next annual meeting. The special meeting must be held in no less than 7 days and no more than 14 days after the supervisory committee has assumed the functions of the board, and candidates may be nominated by petition or from the floor. However, if the next annual meeting has already been scheduled and will occur within 45 days of when the supervisory committee assumes the board's role, the committee may decide to forego the special meeting and wait until the annual meeting to elect new directors. In that event, the



supervisory committee will continue to serve as the board until the new directors are elected at the annual meeting.

If the next annual meeting has not been scheduled but is due to occur within 45 days after all the director positions became vacant, the supervisory committee acting as the board may decide to forego the special meeting and wait until the annual meeting to elect new directors. The supervisory committee will serve as the board until the directors are elected at the annual meeting.

If a special meeting is held and directors are elected to serve until the next annual meeting but the annual meeting has not yet been scheduled, the annual meeting must be scheduled to occur within 7 days of when the last annual meeting occurred in the previous year.

Except in exigent circumstances, the supervisory committee generally will not act on policy matters. However, directors elected at special meeting have the same powers as a board elected at the annual meeting.

CUNA supports changes to Articles XVI and VI of the Bylaws to make them consistent with the changes in Article IX. CUNA also supports the proposed change to streamline the bylaw amendment process by including approved amendments on NCUA's website and to require regional offices to review and provide notice regarding a proposed amendment within 15 days. CUNA agrees with NCUA that credit unions seeking to change the number of members needed for a special meeting should seek a bylaw amendment rather than the agency adopting additional changes to that bylaw for all federal credit unions.

## **Conclusion**

In closing, CUNA supports the agency's decision to bring bylaw enforcement issues to the forefront and appreciates the opportunity to express its views on the agency's proposal. We urge the Board to withdraw the rulemaking and instead, make changes to the Introduction to the FCU Bylaws to clarify the agency's role in addressing bylaw disputes. We support the proposed bylaw amendments, with recommended revisions, regarding the role of the supervisory committee to

assume board functions when all board positions become vacant simultaneously. If you have questions about our comments, please feel free to contact me at 202-508-6736.

Sincerely,

A handwritten signature in cursive script that reads "Mary Mitchell Dunn". The signature is written in black ink and is positioned to the left of a vertical red line.

Mary Mitchell Dunn  
CUNA Deputy General Counsel and  
Senior Vice President

### **CUNA GUIDELINES FOR THE NCUA BOARD ON THE ENFORCEMENT OF FEDERAL CREDIT UNION BYLAWS**

The CUNA Examination and Supervision Subcommittee developed the following guidelines for bylaw enforcement which have been reviewed by CUNA's Governmental Affairs Committee and adopted as policy by CUNA's Executive Committee. These guidelines recognize that NCUA has the legal authority to enforce bylaws, but due to number of practical and operational concerns, they oppose NCUA's enforcement of bylaws that do not address members' fundamental rights and merely address administrative issues. The guidelines also seek to preclude the potential for NCUA examiners to intrude, under the auspices of bylaw regulation, into the daily affairs of a credit union.

- NCUA should recognize that every federal credit union may choose to develop an internal process for handling bylaw disputes.
- NCUA should allow a federal credit union to utilize its internal credit union process first before the agency becomes involved in a bylaw dispute.
- More specifically, NCUA should become involved in the enforcement of a federal bylaw only when a bylaw dispute cannot be resolved within the credit union before turning to NCUA.
- When NCUA becomes involved in bylaw enforcement, its authority should be narrowly construed and should not address bylaws that are strictly ministerial in nature.

- NCUA examiners should be prohibited from involvement in any bylaw disputes, and bylaw compliance should not be integrated into the examination process.
- When an unresolved dispute occurs regarding the enforcement of a core-issue bylaw, the appropriate NCUA regional director should review the dispute. The regional director's decision should be appealable to the NCUA central office.
- NCUA's enforcement of the bylaws should not impose greater regulatory burdens on federal credit unions and should not be more expansive than that of other regulators.