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**Via Email**

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

Re: Comments on Proposed Changes to FCU Bylaws

Dear Ms. Rupp:

We are writing to provide comments in response to the July 15, 2005 Notice and Request for Comments on updating the Federal Credit Union (FCU) Bylaws. Farleigh Witt represents hundreds of credit unions both state and federal, on the west coast and throughout the country. However, we write on our own behalf, and not on behalf of any particular credit union or other client.

**1. Regulatory Relief.**

NCUA's proposed model bylaw changes for FCUs is a prime example of an area in which the NCUA can ease the burden of unnecessary regulation on well capitalized, well managed credit unions. FCUs, like their state chartered credit union counterparts, should have the freedom and flexibility to prepare and implement bylaws and corporate governance guidelines tailored to their specific needs.

Section 108 of the Federal Credit Union Act expressly provides that NCUA board prepare "a form of bylaws, consistent with this chapter, which shall be used by federal credit union incorporators and shall be supplied to them upon request." The statute requires NCUA approval of FCU bylaws at incorporation, but makes no mention of approval of subsequent changes. It is clear this language provided a starting point for FCUs to draft and implement bylaws and was not intended as a regulatory constriction. Restricting FCUs to only the model bylaws is an unnecessary intrusion into corporate governance.

Consistent with a plain reading of Section 108, NCUA has the opportunity to provide regulatory relief to well capitalized, well managed FCUs by permitting FCUs to prepare

and implement bylaws and corporate governance guidelines appropriate to each credit union's size, complexity, and membership. FCU time and effort spent reviewing a limited number of bylaw amendment options or pursuing the required regulatory approval for bylaw amendments on a case by case basis is inefficient and unnecessary. The cost to a FCU of attempting to make a number of necessary updates and changes is many times what a state chartered credit union might spend implementing entirely new, complete and comprehensive bylaws.

**2. Parity with State Chartered Credit Unions.**

We do not agree with the NCUA that the uniformity of model FCU bylaws "enhances" the significance of the federal charter. In fact, our experience is that the mandatory model FCU bylaws is an increasingly important factor that diminishes the significance of the federal charter and further separates FCUs from state chartered credit unions. Many states permit state chartered credit unions of all sizes to prepare and implement bylaws without regulatory intervention or approval and this process has worked extremely well for such state chartered credit unions. FCUs would benefit from the same relief from unnecessary regulatory oversight. We believe FCUs would be best served by a bare-bones approach that sets forth minimum requirements that bylaws must include, with freedom to draft and implement additional bylaws that best fit each organization and its corporate governance needs. Until FCUs gain parity with most state chartered credit unions on this issue, "bylaw freedom" may be one factor that attracts FCUs to a state charter.

**3. One Size Does Not Fit All.**

There is an amazing diversity among FCUs with respect to size, location, field of membership, history, culture, and other matters that factor into corporate governance issues. A $5 million credit union whose membership is primarily concentrated in a small, inner-city neighborhood operates differently than a $500 million community credit union whose membership is spread over four or five large counties. Both of those credit unions would be different from a $3 billion credit union serving members across the country. The management structure for each of these credit unions is likely different from the others. The way in which members participate in credit union affairs is also likely different among these three credit unions. Given that fact, it only makes sense that the three credit unions would be free to adjust their bylaws as necessary to reflect the specific needs of their respective memberships. The current "one size fits all" bylaw requirements should be abandoned in favor of more flexibility for credit unions to satisfy their specific needs.

**4. Specific Bylaw Changes.**

Over the years, we have worked with a number of credit union clients (state chartered credit unions) in totally revising and updating comprehensive and complete bylaws that

focus on a well-managed corporate governance structure and eliminate provisions that are operational or are simply a legacy from previous model bylaws. Much "historical" bylaw content is outdated or is drawn from for-profit corporate law without appropriate adjustment. In reviewing NCUA's proposed model bylaws, we have noted many areas that should be reconsidered, reorganized, and revised to provide a more consistent and comprehensive corporate governance document.

**a. Article II, Section 2.** Member Application Procedures. A number of outdated references remain in this section that are followed by few, if any, FCUs and should be deleted:

- The requirement for the Board of Directors to approve membership application forms is archaic and should be deleted. The credit union's board should be concerned with long-term goals and strategy of the credit union and its financial condition and sound operation rather than with forms design.

- Although Section 109 of the Federal Credit Union Act refers to payment of "the initial installment" of a share of the credit union's "stock," the reality in most credit unions today is that they have a low par value, and no provision for formal payment of "installments." The second sentence in Section 2 should read: "The applicant is admitted to membership on approval by an authorized credit union official after satisfying any requirements set forth in these bylaws."

- A (uniform entrance) fee should be revised to "membership fee" (again despite the archaic reference in Section 109);

**b. Article II, Section 3.** Maintenance of Membership Share Required. This section is inconsistent with Article III, Section 3. In addition, this article does not provide adequate or complete provision for "suspending member's rights for members failing to satisfy or violating membership or bylaw requirements. It is unclear whether a credit union that follows the instructions in Section 4 and specifies restrictions needs to follow the NCUA approval process for case by case amendments. This article should be reorganized to include member expulsion provisions under Article XIV so that all membership qualification, rights and responsibilities are contained in one section.

c. **Article II, Section 4.** The proposed addition regarding limitation of services for members who are "disruptive to credit union operations" should be either reworded or (preferably) deleted. FCUs have long understood that they have the power to restrict or terminate services to members and joint account owners. Specifying requirements or circumstances for such restrictions in the bylaws may simply provide an opportunity for a member to dispute whether the credit union's actions fall within the bylaw provisions. Credit unions should be free to establish (by policy or by bylaws) circumstances under which services to members will be limited.

d. **Article III, Shares of Members.** There are a number of changes that should be considered in this Article:

i. **Section 1.** References to "installments of at least $______" are often no longer relevant, especially for credit unions that have a $5 par value.

ii. **Section 3.** The language related to some delayed payment is outdated and does not reflect current operational practices. In addition, this provision is not consistent with Article II, Section 3. Finally, this section provides for the term "terminated from membership," for which there is no guidance. It is unclear whether a terminated member must also be expelled under Article XIV and if denied, membership must be afforded the same written explanation required under Article II, Section II.

iii. **Section 4.** This section is unnecessary, and reflects a reference to corporate law that is generally inapplicable to credit unions.

iv. **Section 5(c).** This section is ignored in practice, reflects loan policy that should be determined by the credit union, and is an unnecessary handling of operational issues in the bylaws.

v. **Section 5(d).** Again, this is purely operational and assumes that a decedent's estate will be subject to administration, which is not always the case. This is an issue for a regulation or general counsel opinion, not the bylaws.

vi. **Section 5(e).** This is not a corporate governance provision but rather a compliance reminder, and should be removed.

vii. **Section 6.** This section is unnecessary and does not address additional types of trust relationships that credit union operations deal with from time to time.

**viii. Section 7.** This section attempts to provide for multiple members in one account. However, the terms such as "joint membership" and "primary owner" should not be used as they inaccurately reflect the actual ownership and membership holding the account. We do not believe the options (a) and (b) adequately address and disclose to the joint owner the various requirements and consequences of not satisfying the membership requirements. For example, joint owners cannot vote, hold office, sign petitions, etc., unless they are also members.

**e. Article IV. Meetings of Members.** The current bylaws (and the proposed revisions) do not adequately address many issues that arise regarding membership meetings. Moreover, while adoption of a particular set of rules of order will provide further guidance to a credit union, most rules of order are inadequate to address many issues that arise in the credit union context due to the unique nature of credit unions. Credit unions should be free to fill these gaps with specific rules of procedure or policies adopted by the board.

For example, the bylaws provide that 15 members constitute a quorum at annual or special meetings. If a credit union does not adopt notice requirements for motions or proposals to be voted on at an annual meeting, a small number of members could easily take an action that the majority of members disapprove of simply by showing up at the annual meeting, making a motion, and voting on it. Again, different credit unions will have different cultures, histories, and styles for annual meetings and other issues. Each credit union should have the flexibility to adopt rules and procedures tailored to its specific needs.

This section could be better organized by creating entirely separate sections for annual meetings and special meetings. As drafted, there are a number of inconsistencies on notice requirements due to combining meeting requirements in one article. Similarly, the reference to rules of procedure and parliamentary procedure in Section IV, seem to apply only to annual meetings and not special meetings.

**i. Section 4.** In Section 4, NCUA should clarify and more completely provide the board with the authority to adopt rules of procedure for meetings and elections, not just parliamentary procedures. In addition, the discussion in the supplementary information (Page 40926) regarding NCUA's long recognized position regarding members voting rights is problematic. Credit unions must be extremely careful in how these types of provisions are drafted in order to avoid conflicts with similar provisions provided in the parliamentary procedural rules. If such provisions are not drafted correctly, it is possible for parliamentary procedures, such as *Roberts Rules of Order*, to confer members' rights that are inconsistent with and far more expansive than provided by these bylaws or a credit unions established practices.

**ii. Section 5.** In Section 5, the quorum of 15 members is unrealistically low and a very dangerous level to establish. Many credit unions permit member action by mail ballot. In an action which thousands of votes have been cast by mail, permitting 15 members to potentially alter the majority view of the membership would be unwise and undemocratic. Credit unions should be able to establish their own quorum levels, perhaps within limits based on the number of members.

**f. Article VI, Section 6.** The establishment of a loan collection program and authorizing charge-offs is more properly a management function that should be overseen by the board, but not performed by the board.

**g. Article VII, Section 4.** This section is unclear as to whether the board must approve individuals who can spend the credit union's money, or individuals who can sign any credit union check (including checks for member account withdrawals, loan proceeds checks, etc.). In fact, this entire section seems like an unnecessary operational matter that can be handled in policy, rather than the bylaws.

**h. Article VII, Section 8.** This section describes an operational structure that is different from many credit unions, and is different from the organizational structure recommend by many organizational experts. In most credit unions, the board employs, reviews, and sets compensation for the CEO. The CEO (and management hired by the CEO) handles employment issues related to all other employees. The wording of this section makes it unclear whether and when the board has such authorities, and can lead to poor communication and structural tensions between the board, CEO, and other senior management. Again, it would be best to delete this section altogether and leave these matters to individual credit unions for determination.

**i. Article 11, Section 2.** This is another operational issue, and should not be in the bylaws.

Revision of the standard bylaws is an important process. We believe that NCUA and FCUs will benefit from a more extended discussion of these issues. One approach would be to extend the comment period for an additional six months. Another approach would be to issue a revised proposal based on comments NCUA has already received, with a long comment period for the revised proposal. In any event, we believe that the NCUA needs more input before adopting new standard bylaws.

We appreciate the opportunity to provide this comment.

Sincerely,

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