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December 21, 2000

Manager
Dissemination Branch
Information and Services Division
Office of Thrift Supervision
1700 G. Street, N.W.
Washington, D.C. 20552

RE: Proposal: 65 F.R. 66116 (November 2, 2000);
Docket No. 2000-93

Dear Sir/Madam:

We write to address, and object to, the proposed rule published in the Federal Register on November 2, 2000, 12 CFR Parts 544 and 552 ("Rule").

The Rule, if adopted, would permit Federal Savings Associations ("Thrifts") to: (i) retroactively expand the qualifications for service on a Board of Directors and establish disqualification factors that are more restrictive than those established by Congress; (ii) disenfranchise shareholders by preventing the nomination of persons to the Board of Directors who are not otherwise disqualified.

In addition, the proposed Rule establishes standards for participation in the operation of Thrifts that should only be created, if at all, through the adoption of regulations.

The pre-approval of the proposed bylaw *per se* encourages Thrifts to adopt it. Implicit in the fact that the OTS has given its imprimatur approval to this new restriction upon the qualifications for membership on a Board of Directors is the notion that this restriction will protect the institution, its members/shareholders and depositors and that failure to adopt the bylaw may be viewed as an unsafe or unsound practice. This implication is fortified by the OTS' statement, which is set forth in the summary section that accompanies the Rule proposal and provides:

> "The proposed preapproved bylaw is intended to permit Thrifts to better protect their business from adverse effects that are likely to result when the reputation of its Board Members does not elicit the public's trust."

Given the tenor of the quoted statement, and the scope of the discretionary power that the OTS can exercise over Thrifts, this "optional" bylaw is tantamount to a directive. As a directive, it would set the standard for Board service not supported by law or a duly promulgated regulation.

We strongly believe, as discussed below, that the proposal is flawed because it seeks to implement significant regulatory standards relating to management competency, and integrity, under circumstances where the OTS has not clearly justified the need to implement standards beyond those established by Congress in the Federal Banking Laws. Further, even if such a justification were presented, a new standard should not be adopted by the OTS as an "optional" or "model" bylaw for Thrifts, but rather as a fully supportable regulation implementing relevant statutory standards or authority. [This does not concede that the OTS has the authority to lawfully adopt new standards for Board membership that are more restrictive than the standards established by Congress. See, e.g. Manges v. Camp et al, 474 F.2d 97 (5th Cir. 1973).]

We fully agree with the OTS' assertions in the preamble of the proposal that "Congress has repeatedly expressed concerns about the character and integrity of the people who control savings associations" and that the OTS also has been concerned "with the character of persons who would hold director positions in [T]hrifts." Where the foregoing concerns have existed, the OTS correctly asserts that the Congress has adopted specific statutory standards to address certain types, and categories, of conduct that would bar a person from Thrift management. Similarly, the OTS in the particular context of chartering new Thrifts, has established certain standards that are consistent with its view that the Directors of new Thrifts must reflect a history of "personal integrity."

Notwithstanding the foregoing, however, the standards set forth in the proposed bylaw, if adopted by a Thrift, would potentially bar a person from serving as a Director under circumstances where such service is clearly permissible under relevant Federal Banking Laws and under the current rules promulgated by the OTS. This conflict with the Federal Banking Laws would *ipso facto* invalidate the Rule. (Manges, *supra*) Further such an anomaly of necessity requires that the OTS justify the legality of such a standard in the context of adopting a regulation addressing the standards applicable to potential director candidates, not the subject proposal. In our view, imposition of such standards through an "optional bylaw" provision is legally defective because it evades addressing the legal authority to impose -- or permit imposition of -- such a standard.

This legal defect is not cured in any meaningful manner by the puzzling argument that the OTS asserts by justifying the proposed bylaw as an "optional" provision for Thrifts that can be used to address management integrity issues. We would point-out that the proposal is not "optional" for a director candidate who seeks to serve on the Board of a Thrift that has adopted this provision. Rather, any director candidate falling within the coverage of the Bylaw will, by definition, be barred from serving on that Board. Where such a candidate would otherwise be legally permitted under the Federal Banking Laws, and under the current OTS rules to serve on such a Board, the OTS must provide a more direct and clear justification for authorizing the Thrift industry to bar such individuals.

As such, the assertion by the OTS in the preamble to the proposal that the "proposed

bylaw standards" are derived "in part" from existing regulatory standards only serves to underscore the obvious: the OTS has not to date fully explored or justified its authority in the context of a rulemaking subject to notice and public comment to impose by regulation the management standards it proposes to permit Thrifts to adopt in the form of a bylaw. In this vein, the OTS should withdraw the proposal until such time as the OTS has proposed for public comment rules explicitly, and fully, justifying the OTS's authority to impose all of the standards set forth in the subject bylaw provision.

Furthermore, the OTS is incorrect in asserting that the proposed bylaw provision "does not bar any one from the industry." On the contrary, the proposed bylaw will act as a bar at each Thrift adopting such a provision where a director candidate falls within the scope of its coverage. Furthermore, this view ignores the established track record of Thrifts-on an industry wide basis-adopting "optional" "model" bylaw as permitted by the OTS. As such, and based on past-experience, the OTS is remiss in not specifically acknowledging the possibility that the proposed bylaw provision may be adopted by large numbers of Thrifts, and thus, act as an industry-wide *de facto* bar to proposed directors falling within its scope.

Due to its unique role as the primary source of corporate governance authority for Thrifts, the OTS cannot pretend that it is not directly adopting a significant regulatory standard relating to management competency, and integrity simply by teeing up the proposal as an "optional bylaw." The fact of the matter is that in proposing such a Bylaw for Thrifts, the OTS is essentially opining that such a provision is legal, not just permissible. Such an assertion of legality must be undergirded by the OTS' own direct authority to impose such standards by regulation, especially in circumstances, as noted above, where such standards may act as a industry-wide ban on certain candidates.

Furthermore, the proposal provides no justification as to why only Federally Chartered Thrifts would be granted the authority to ban persons from Boards under the circumstances prescribed. Given the OTS' regulatory jurisdiction over a substantial number of State Chartered Thrifts, it is unclear whether the OTS would object to state chartered thrifts adopting similar standards, and if so, under what authority or circumstances. Notably, if the OTS limits the scope of its proposal to Federally Chartered Thrifts it will be creating a troublesome situation. Under the rubric of statutory authority established under the Federal Banking Laws governing management competency and integrity standards directly applicable to both Federal and State Thrifts in an equal manner and without differentiation, the OTS will be vesting Federally Chartered Thrifts with extraordinary authority not available to State Chartered Thrifts. Such a potential result is arguably inconsistent with the statutes at issue, and at minimum, must be specifically justified under circumstances where the public is given notice and the opportunity to comment.

It is submitted that there is no data, nor experiential evidence, to support the claim that the inclusion on a Board of Directors of a person who was subjected to the Cease and Desist Order ("C&D"), described in the proposed Rule, within the prior ten (10) years, has resulted in any adverse consequences. The available data does not disclose the existence of any situation where a Thrift has suffered any adverse consequence (for example: loss of deposits, reduction in profits or drop in stock price) due to the membership on its Board of Directors of a person who has been subject to a C&D. In fact, within the last three years several Thrifts

have had a person elected to their Board, who was currently subject to a C&D, and the results of that persons' participation in the Thrift were demonstrably positive.

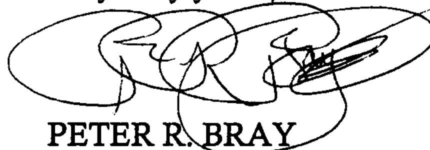
This Rule, as promulgated, would disqualify persons who are currently subject to a C&D and otherwise qualified to serve on the Boards of Directions of Thrifts. As a result, the rule would have a retroactive effect, which violates the Administrative Procedures Act. 5 U.S.C.§ 551(4); Bowen v. Georgetown University Hospital, 488 U.S. 204 (1988). In effect, this Rule encourages Thrifts to adopt this Bylaw and convert a C&D into a Bar and Prohibition Order -- disqualifying persons whom Congress has determined are qualified to serve. This *ex post facto* change in the qualification standards is patently illegal, and its application is both arbitrary and irrational. For example, this Rule permits the disqualification of persons who consensually entered into C&Ds, believing same would not be -- and could not be -- used as a tool to bar their participation in this industry. Furthermore, the reach of this rule would encompass persons who have had a C&D vacated and discharged by the OTS.

As promulgated this rule states that one class of persons affected are those who have been subjected to a C&D for "dishonesty" or "breach of trust." This standard is beyond the scope of the statute, which unambiguously stipulates that a C&D is issued when an institution-affiliated party has engaged in an unsafe or unsound practice. 12 U.S.C.§1818(b) In fact, Congress has specifically reserved Bar and Prohibition Orders for situations involving dishonesty and breaches of trust. 12 U.S.C. §1818(e)

The Rule, in application, would only serve to limit the choices available to shareholders and concomitantly serve as a tool for management entrenchment. This is borne-out by some very obvious facts: (i) A mutual association would not bother to adopt this by law, since its management can exclusively control the composition of its Board of Directors; (ii) A publicly-held association (approximately 30 currently exist) would consider adopting this bylaw -- not to control the type of persons who could serve on the Board, since this is subject to management's control in uncontested situations -- but only to prevent shareholders from nominating a person for election in a proxy contest.

We urge the OTS to not adopt this Rule for the reasons discussed above. As drafted this Rule will not serve any legitimate purpose, will have a detrimental effect and will be illegal.

Very truly yours,



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