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FROM: Acting Assistant General Counsel
Hattie M. Ulan

SUBJECT: Nonstandard Bylaw Amendment
(Your October 28, 1988, Memo)

DATE: December 1, 1988

You have asked for our comments on a proposed nonstandard bylaw amendment ("the proposed amendment") to Article VI of the FCU Bylaws. The proposed amendment would alter Article VI by adding a Section 9 to prohibit an FCU employee from serving as a member of the board of directors or supervisory committee while employed by the FCU and for a period of two years following termination of such employment. You indicated that you were inclined to deny the portion of the proposed amendment pertaining to a prohibition against a former employee serving as a director for a period of two years after termination of their employment, but were inclined to grant the portion of the proposed amendment regarding the prohibition against an employee serving as a member of the supervisory committee while so employed and for a period of two years following termination of employment with the FCU. We agree.

BACKGROUND

The FCU has requested that a Section 9 be added to Article VI of the bylaws to provide as follows:

No employee of this credit union may serve as an elected or appointed member of the Board of Directors or Supervisory Committee. Such prohibition will remain in force and effect for a period of two years following termination of employment with this credit union.

The FCU states that the purpose of this proposed amendment is to prevent employees of the credit union from being elected to the board of directors or appointed to the supervisory committee while they are employees and for a two year period thereafter. The FCU has not provided any further explanation of the need for the proposed amendment. It does note that the proposed amendment is the reverse of a standard amendment to Article VIII, Section 7 of the Bylaws that provides, in part:

. . . no director or committee member may be a paid employee of this credit union for a minimum of two years from the date the official terminates his/her position as a director or committee member unless the employee position to be filled exists as the result of a death or disability. (See p. 11 of NCUA publication 8001A.)

The stated purpose for this Standard amendment is that it:

diminishes the possibility of "insider" dealings to take advantage of a position of authority. For example, it may prevent abuses such as the board of directors discharging the manager to create a vacancy for a credit union director to be hired. (See p. 11 of NCUA publication 8001 A.)

ANALYSIS

In addition to the standard bylaw amendment cited above (hereinafter referred to as the first standard bylaw amendment), there are two other standard bylaw amendments that bear on this issue. One provides that ". . . no director or committee member or member of the immediate family of a director or committee member may be a paid employee of this credit union." (See p. 10 of NCUA publication 8001A.) This amendment (hereinafter referred to as the second standard bylaw amendment) is permitted for purposes of internal control. The third standard amendment bearing on this issue is a variation of the second standard bylaw amendment. it provides ". . . no more than _____ directors may be paid employees of this credit union." (See p. 10 of NCUA publication 8001A.) This amendment provides the

board of directors with the discretion of limiting the number of directors that may be paid employees of the FCU.

The FCU is correct in stating that the proposed amendment is the reverse of the first standard bylaw amendment. The first standard amendment places a limitation on a director or committee member's ability to become an employee of the FCU. Conversely, the proposed amendment places restrictions on an employee's ability to become a director or committee member.

Prohibition Against Employee Serving as Director

As you are aware, it has long been our position that the only eligibility requirements for FCU board membership are those contained in the FCU Act and the Bylaws. That is, as long as an individual is a member (Section 111 of the FCU Act) and has not been convicted of a crime involving dishonesty or breach of trust (Section 205(d) of the FCU Act), or if they have been convicted of such a crime the NCUA Board has waived the Section 205(d) prohibition, he or she is eligible to be elected as a director. Article VI, Section 7 of the FCU Bylaws also permits the board to establish a minimum age requirement. NCUA has generally not granted nonstandard bylaw amendments in this area.

The amendment sought by the FCU would prohibit an FCU employee from serving as a director while he or she is working for the FCU and for two years thereafter. The second standard bylaw amendment permits an FCU to prohibit a director or committee member from being a paid employee of the FCU. NCUA has allowed this amendment since (1) it does not bar an individual from board or committee membership; it simply requires the individual to determine whether he or she wants to be a paid employee or on the board of directors; and (2) it promotes principles of sound internal control. The proposed bylaw amendment goes a step further from this standard amendment in that it continues the prohibition for two years after termination of employment. In our view, this prohibition is impermissible as it serves as an absolute, albeit temporary, bar against an FCU member serving as a director during the two-year period.

The proposed amendment is distinguishable from the first standard bylaw amendment, which is a prohibition against a director serving as an employee. It does not limit eligibility for board membership. We concur with your decision to deny the request with respect to a prohibition against former employees serving as directors. The FCU may, of course, adopt any of the standard bylaw amendments.

As you are aware, while we do not believe that the FCU should be permitted to adopt this portion of the proposed amendment, the FCU's nominating committee may consider the fact that an individual was an employee of the FCU in deciding against including the person as a nominee. This is inherent in the discretion given to the nominating committee by Article VI of the Bylaws.

Prohibition Against Supervisory Committee

The proposed amendment also restricts credit union employees from serving as supervisory committee members while they are so employed and for two years thereafter. Since a position on the supervisory committee is not an elected position, the free choice of the members would not be impaired by such a provision. Article X, Section 1 of the FCU bylaws presently provides in part that "[n]o member of the credit committee or any employee of this credit union may be appointed to the (supervisory) committee." We see no legal impediment to amending this bylaw to continue the prohibition against employees serving on the supervisory committee for two years after their employment is terminated. Since it is a policy decision, we will defer to your judgment on this issue. We do agree that the amendment, if granted, seems more appropriately located in Article X rather than Article VI.