

GC/MRS:sg

SSIC 6100

92-0522

[ ]

FROM: Hattie M. Ulan, Associate General Counsel

SUBJ: Nonstandard Bylaw Amendment, [ ] (Your May 11, 1992, Memorandum)

DATE: June 15, 1992

[ ] has requested approval of a non-standard amendment to Article III, Section 3 of its bylaws, which deals with termination of the membership of an FCU member who fails to pay or maintain one full share in his account. The standard bylaw provides for termination in several cases, including when the member reduces his share balance below the par value of one share and does not increase the balance to at least one share within the time set forth in the bylaw. The standard bylaw allows the FCU to select the time period, but requires that the member be given a minimum of six months.

[ ] proposes to eliminate the six month waiting period before terminating the membership of a member who has reduced his shares below the par value of one share. The proposed amendment would make an exception in cases where the reduction occurs due to levy or court order.

We would not support an amendment that allows termination of membership sooner than the six month minimum prescribed by the standard bylaw. Although not required by the FCU Act or the Regulations, the six month minimum was established by the NCUA Board when it promulgated Article III, Section 3 as a standard amendment in 1982 (see Letter to Credit Unions No. 70), and therefore represents Board policy. Since this proposed bylaw amendment would affect members' fundamental rights, we do not believe that the minimum standard set by the Board should be changed by this Office or by the Regional Offices; in our view, any change would have to come from the Board.

Your memorandum analyses the proposed amendment in terms of the expulsion for nonparticipation provisions of Section 118 of the FCU Act. We do not agree that the bylaw's termination provisions are based on nonparticipation. The standards for termination of membership under the bylaw and expulsion under Section 118 are not the same. Furthermore, we doubt that the actions described in the bylaw would constitute nonparticipation.

You suggest that, as an alternative to the proposed amendment, [ ] could adopt an expulsion policy under Section 118, based on the same criteria that it proposed for the amendment. However, you question whether an FCU may expel a member for nonparticipation based on his failure to maintain a balance of at least one share, without giving him the minimum six months to bring his account back up to par. We do not think that an FCU has that right. While nonparticipation is not defined in the Act, the term suggests some continuing failure to take an interest in the FCU or use its services. In the past, we have said that nonparticipation is the failure to use FCU share, loan or other services "for a period of time." We are not prepared to say that reduction of an account below par value, by itself, can ever constitute nonparticipation. However, assuming that it can, it seems to us extreme to say that a member fails to participate in an FCU the instant that he reduces his share balance below par value. This is especially true where, as here, the FCU's shares have a relatively high par value of \$100. In our view, the member must be given a reasonable amount of time to return his account balance to the necessary minimum before losing his membership.

In this case, six months is the minimum that would qualify as a reasonable amount of time. Otherwise, an FCU would be able to do with a nonparticipation policy what it could not do under its bylaws, that is, terminate of an individuals membership for reduction of his account balance below par, without the minimum six month waiting period. Again, in light of the Board's policy requiring the six month period, it would be inappropriate to allow a nonparticipation policy with a shorter time frame.

You indicate that if you do not approve the proposed amendment, [ ] will implement a policy of expulsion for nonparticipation, pursuant to Section 118, under which a member will be expelled if he fails to return his share balance to at least par value within six months of having reduced it. As we stated above, we do not believe that reduction of an account balance below par qualifies as nonparticipation. Even if we did agree that such a reduction amounted to nonparticipation, implementation of the policy proposed by [ ] would be redundant. We assume that [ ] presently has the standard bylaw in place. Therefore, under, [ ] current bylaw, a member who fails to bring his account back to par within six months will already have his membership terminated. We see no need for [ ] to create a separate policy to accomplish this same result.

We understand that [ ] may find accounts with balances that frequently dip below par value to be both expensive and an administrative burden. As an alternative to the proposed amendment, [ ] could impose a fee on accounts that fall below a set minimum, i.e. the \$100 par value. We have previously permitted FCUs to offer minimum balance accounts and charge fees when the accounts fall below the minimum balance. We have also stated that an FCU need not offer a "regular share account," but may require its members to maintain minimum balance accounts in order to establish membership. We have attached a copy of an earlier memorandum discussing minimum balance accounts and fees. [ ] may wish to consider this option.

Attachment (below)

GC/MRS:sg

SSIC 3600

91-0206

[ ]

FROM: Hattie M. Ulan, Associate General Counsel

SUBJ: [ ] - Minimum Balance Fee

DATE: February, 28, 1989

You requested a legal opinion on the following issues raised by the [ ] 1. May [ ] take away membership by absorbing the par value of a member's "primary" share account through application of a minimum balance fee? 2. May [ ] require a member who has no balance in his "primary" account to pay off his loans and/or close his savings account? Briefly, our answers are as follows.

1. Yes, provided that [ ] has given, the member the requisite opportunity to bring his share balance up to par value, as required by Article III, Section 3 of the Standard FCU Bylaws. 2. A member may not be required to pay off his loans, but under certain circumstances he may be required to close his savings accounts.

## **Analysis**

### **1. Minimum Balance Account**

Section 109 of the Federal Credit Union Act (12 U.S.C. §1759) requires an individual seeking membership in an FCU to "subscribe to at least one share of . . . (the FCU'S) stock and pay the initial installment thereon." Both your memorandum and [ ] letter refer to the member's "primary" account. We note that neither the Act nor the NCUA Rules and Regulations defines or uses the term "primary account," and we have not found the term in the Accounting Manual. We assume that both you [ ] and mean "primary account" to indicate the account that an individual opens by subscribing to a share in order to become a member of an FCU, and for purposes of this letter we shall give the term that meaning.

You appear to be under the impression that the member's primary account must be a regular share account. That is not

the case. We have recently opined that an FCU is not required to offer a regular share account in order to establish membership. Section 109 merely states that an individual must subscribe to a share of stock and pay the initial installment thereon; it does not dictate that the one share be in a regular share account. Neither the Act nor the Regulations precludes an FCU from requiring an individual to establish membership in the FCU through an account other than a regular share account. Moreover, Section 5150.2 of the Accounting Manual states, in part:

A regular share account does not have to be established in order for a person to become a member of a credit union. The board of directors of each federal credit union decides what is best for the characteristics of its own membership. For example, the board of directors may decide that -membership qualification can be accomplished by the establishment of a regular, notice, split-rate, minimum balance, share draft, or share certificate account.

While we do not believe that an FCU could require an individual to meet any minimum balance requirement (as opposed to par value requirement) in order to establish membership, it does not appear to us that [ ] imposes any such rule upon its members; we assume that [ ] described the account's minimum balance requirements solely in order to explain why the account was reduced below par value. As we understand it, [ ] requires only that an individual subscribe to and purchase one share of stock at the \$5 par value in order to open the account and become a member; the \$100 minimum balance requirement simply allows Census to deduct a service fee when the share balance is below the minimum. Membership is dependent not upon maintaining the \$100 minimum, but upon maintaining the \$5 par value. [ ] may legally offer the minimum balance account described in its letter, and that account may operate as a primary account, that is, an account that establishes the member's membership in [ ]. You did not request any opinion on the requirements for payment of dividends on a minimum balance account such as that described by [ ]. We have attached an earlier opinion addressing payment of dividends, for your information.

The real issues seem to be these: (1) whether an FCU may impose a minimum balance fee on an account whose minimum balance is greater than par value and, if so, (2) whether, when application of a minimum balance fee absorbs funds in a primary account to the point that the share balance falls below par value, an FCU may terminate the account holder's membership. Our answer to both questions is a qualified yes.

Nothing in the Act or the Regulations requires that par value be established at more than \$5, or be equal to the stated minimum balance required for an account, before a minimum balance fee can be imposed. Imposition of fees to accounts is governed by Section 701.35 of the Regulations (12 C.F.R. §701.35). That section states, in part:

(c) A Federal credit union may, consistent with this Section, other Federal law, and its contractual obligations, determine the type of disclosures, fees or charges, time for crediting of deposited funds, and all other matters affecting the opening, maintaining or closing of a share, share draft or certificate account. State laws regulating such accounts are not applicable to Federal credit unions.

Section 701.35(c) does not restrict the minimum balance policies of FCUs setting fees. We see no reason why [ ] may not deduct a \$1 fee from an account when the share balance in that account falls below the \$100 minimum balance, even to the point of reducing the share balance below par value. The amount of the fee and the policy regarding its imposition must be clearly set out in the account agreement. Moreover,

[ ] must comply fully with Section 701.35(b) of the Regulations (12 C.F.R. §701.35(b)), which requires an FCU to "accurately represent the terms and conditions of its share, share certificate and share draft accounts in all advertising, disclosures, or agreements, whether written or oral."

While [ ] may impose the minimum balance fee, it may not automatically terminate an account holder's membership when application of the fee reduces his primary account balance below par or to zero. Article III, Section 3 of the Standard FCU Bylaws requires that a member whose share balance is reduced below par be given a specified time to increase the balance back to at least par value before his membership may be terminated. We have consistently interpreted Article III, Section 3 to apply when the share balance is reduced due to absorption by fees imposed by the FCU. The individual FCU must specify in its own bylaws the time an individual will be granted for increasing his balance to par, but the standard bylaw requires a minimum period of six months. Therefore, before an individual holding a minimum balance account at Census, whose share balance has been reduced below par value (\$5) can be terminated from membership, he must be given six months (or such greater time as may be provided by Article III,

Section 3 of [ ] bylaws) to raise his share balance to at least par value.

Letter to Credit Unions No. 72, dated November 29, 1982 indicated that since Article III, Section 3 may result in loss of membership if payment of one share is not completed within the specified time frame, FCUs should notify their members of the bylaw and what they must do in order to avoid adverse consequences. While we have not required that a member be notified every time his share account is reduced below par value, members should be made aware of the FCU's policy of closing an account that falls below par value due to absorption through fees, and terminating the account holder's membership. Again, we refer you to Section 701.35(b) of the Regulations.

## 2. Requiring Member to Pay Off Loans and Close other Accounts

An FCU has no right to force an individual to pay off a loan simply because his membership in the FCU has been terminated. Repayment of a loan is governed by the repayment terms set out in the loan contract, and an FCU may not unilaterally amend that contract. Neither the Act nor the Regulations provides any basis for accelerating a loan solely on the basis of termination of membership.

[ ] may wish to amend its loan agreement forms so that future contracts would provide that payment in full was due upon termination of membership. If so, [ ] must comply with Section 701.35(b). We are not endorsing such a change; we are merely stating that loan termination procedures must be part of the loan contract. Enforceability of the loan agreement would be determined under state law. We offer no opinion as to whether the amended agreement would be enforceable under the law of Washington, D.C. (where Census has its main office) and/or Indiana (where the branch office is located). [ ] should obtain an opinion from its own counsel on that issue .

With regard to closing out all other share accounts of a member when the share balance in his primary account has been absorbed, we fail to see why [ ] would wish to do so. However, such a course of action is not necessarily illegal. An FCU's right to require a member whose primary account has been absorbed to close his other share accounts would depend upon the FCU's stated membership policy and the way that the accounts are structured. For example, if the FCU's account structure were such that a member had to have a primary account of the type described in Part 1 of this memorandum in order to qualify for membership and maintain any other accounts, then the FCU could close the other accounts when the member's primary account had been absorbed and his membership terminated. We believe that an FCU could transfer the funds in the member's accounts to accounts payable and then pay them to the member. We refer you to the Accounting Manual for further guidance in this area.

On the other hand, if the membership policy and account structure required only that the member maintain shares of par value in some account, the FCU would not have the right to close his other accounts no matter what happened to the primary account. We do not have sufficient facts before us to give an opinion on the course of action proposed by Census.

In the event that [ ] chooses to implement a policy whereby a member's accounts are closed when his membership is terminated because the share balance falls below par value (and after the six month or greater period prescribed by Article III, Section 3 of the Bylaws), the board of directors should make a resolution to that effect. Again, [ ] should take care to accurately disclose any such policy, in accordance with Section 701.35(b) [ ] would have to disclose its policy to all future members, and might wish to set forth the policy in its newsletter or a statement insert, for the information of current members, who would otherwise be unlikely to learn of the policy. We would also note that such a policy must be consistent with share account agreements currently in use (e.g. share agreements must allow for such a unilateral change, if it is a change).

Attachment