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November 29, 2004

Ms. Mary F. Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Re: National Credit Union Administration; Federal Credit Union Bylaws; 69 **Federal Register**, 58203, September 29, 2004

Dear Ms. Rupp:

The American Bankers Association ("ABA") welcomes the opportunity to offer its comments on the proposal to update, clarify and simplify the Federal Credit Union Bylaws published by the National Credit Union Administration ("NCUA"). The ABA appreciates NCUA's efforts to include corporate governance practice in the Federal Credit Union Bylaws, in accordance with the standards laid out in the Sarbanes-Oxley Act of 2002 ("Act"). The ABA's letter will primarily focus on this aspect of NCUA's proposal while suggesting specific modifications to the Federal Credit Union Bylaws Manual.

The ABA brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership—which includes community, regional, and money center banks and holding companies, as well as savings associations, trust companies, and savings banks—makes ABA the largest banking trade association in the country.

Background

In its proposal, NCUA recommends several modifications to its existing Federal Credit Union Bylaws. These include membership treatment of joint account owners, order of business procedures during meetings, election procedures and definition of "compensated officer". In addition, NCUA seeks comment on improvements in corporate governance especially relating to the application of the Act's concepts on credit unions.

In terms of the Act's impact on banks' corporate governance policies, the Securities and Exchange Commission ("SEC") has worked since the Act was enacted into law in the summer, 2002 to adopt numerous final rules to implement various provisions of the Act. The bank regulators have issued subsequent guidance regarding the application of the Act to large banks, as well as to small and non-public banking institutions. [1]

ABA Position

ABA supports the corporate governance principles laid out in the NCUA's own guidance, issued in October, 2003. [2] Specifically, ABA believes that the largest and most complex credit unions should be required to comply with the principles of the Act to the same extent that similarly situated banks are required to comply. In addition, the NCUA should provide guidance on good corporate governance to smaller institutions similar to those suggested by the federal bank regulators. The following provides a brief summary of the governance standards banks are expected to uphold. These standards should serve as a framework for compliance by credit unions.

Bank Governance Standards

Code of Ethics

The SEC's final rules require a company to disclose whether it has adopted a code of ethics that applies to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions. If the company has not adopted such a code of ethics, it must explain why it has not done so.

The Federal Deposit Insurance Corporation ("FDIC") has encouraged all institutions under its supervision to adopt internal codes of conduct that, among other things prohibit bank officials from self-dealing or otherwise trading on their positions within the bank. In addition, the FDIC recommends that banks' codes of conduct require officials to disclose all potential conflicts of interest, including those in which they have been inadvertently placed due to either business or personal relationships.

[1] FDIC Financial Institution Letter FIL 17-2003, FIL 122-2004
[2] NCUA letter to Federal Credit Unions No. 03-FCU-07

Conflicts of Interest /Auditor Independence [3]

In its guidance, the FDIC encourages that for banks under $500 million in assets, when the bank's external auditor is hired to perform both internal auditing and accounting to pay particular attention to "preserving the independence of both the internal and external audit functions."

The FDIC also recommends that the audit committee consider how the bank will oversee the external auditor's performance.

Federal banking laws require banks with assets in excess of $500 million and strongly encourage banks with assets under $500 million to establish independent audit committees.

Corporate Responsibility for Financial Reports

According to the FDIC, banks that issue audited financial statements to their shareholders or others may also want to consider including with the financial statements a certification by the bank's principal executive officer and principal financial officer. The certification would state that the officers have reviewed the financial statements and, based on their knowledge, the statements are true and fairly present in all material respects the bank's financial condition, results of operations, and cash flows.

Improper Influence on the Conduct of Audits

The FDIC strongly encourages compliance with Section 303 regardless of the type of external auditing program an institution has implemented. Improper influence over external auditing work may be deemed an unsafe and unsound practice.

Internal Controls

Under the Federal Deposit Insurance Corporation Improvement Act ("FDICA"), banking institutions of a certain size are required to evaluate internal controls, report on them, and obtain an external auditor's assessment of management's reporting.

[3] In terms of the impact of NCUA's conflicts of interest regulations on credit unions, the ABA encourages NCUA to more vigorously enforce its existing conflicts of interest regulations (12CFR 701.21, 715, in particular). ABA is aware of instances where credit unions converting to mutual savings bank charters are surprised by the seriousness with which the federal banking regulators view repeated or long-tolerated Regulation O type violations.

However, as the 2003 Government Accountability Office ("GAO") study points out, "credit unions are not subject to the internal controls and attestation reporting requirements applicable to banks and thrifts." GAO goes on to say that "reports on management's assessment of the effectiveness of internal controls and the independent auditors attestation of management's assessment have become normal business practice for financial institutions and most businesses."

Improve Federal Credit Union Corporate Disclosures

In addition, ABA reiterates its position that credit unions need to improve their corporate disclosures. ABA recommends that NCUA adopt the following:

- Require annual disclosures of all senior management's compensation and benefits to credit union members and a positive vote of the board's independent (not members of senior management) members to approve such compensation.
- Disclose whether or not the board of directors is independent from credit union management, the number of "inside" or senior management officials that serve on the board of directors, and the qualifications of board members including whether or not anyone with financial expertise is a member of the board.
- Disclose all benefits received by credit union boards of directors.
- Require credit unions to disclose whether their auditor is independent and the availability of that audit to credit union members.
- Report the capital ratios of the credit union both with inclusion of the National Credit Union Share Insurance Fund contribution and without.
- Disclose all regulatory actions that are active and in force taken against the credit union, its employees or management.

Such disclosures would begin to bring credit unions into parity with what is required by other federal depository regulators and improve the transparency of credit union management, including the boards of directors. Such knowledge would allow credit union members to vote in an informed manner for board members and provide a more informed basis for choosing membership among credit unions. Informed depositors choosing financially strong credit unions reinforce the NCUA's regulatory effectiveness.

Suggested Federal Credit Union Bylaw Modifications

The ABA is concerned with NCUA's apparent attempt to impose unnecessary costs and burdens on the election process through use of independent third-party tellers.

The use of such independent third-parties can add significant delay to the election process and impose substantial additional expenses on credit unions in their administration of elections. Further, while confidentiality and secrecy in voting may give some credit union members greater confidence in their vote, strict compliance with such rules may also serve to actually *discourage* voting. For instance, if a member would like to vote by handing his or her ballot to a teller (folded over and stapled or taped), the NCUA's secrecy and confidentiality requirements would require the teller to refuse to take the ballot because it had not been mailed to the independent, third-party vote tabulator.

Rather than add barriers to voting, we encourage NCUA to simplify the election process and to facilitate voting through convenient, member-friendly means including allowing members to drop off their ballots at a branch or other credit union facility. This is in better keeping with the members' interests in the governance of their credit unions.

In undertaking its overall review of the Federal Credit Union Bylaws, the ABA recommends that NCUA revisit its existing prohibition against allowing members to vote by proxy. As NCUA seeks to expand voting opportunities by its proposal to allow trustees to vote contrary to its existing prohibition, it should also recognize that in today's world, proxy voting is universally recognized as an appropriate option for individuals and organizations. NCUA should update its Federal Credit Union Bylaws Manual to recognize this legitimate means for members to vote.

Finally, the NCUA proposes an optional bylaw that would require each joint account holder to have a separate account in order for each account holder to be eligible for membership and thereby eligible to vote. This option would have the result of disenfranchising a significant segment of credit union accounts (e.g., married account holders). Rather than have these members go through the expense and administration of additional accounts for the sole purpose of being able to vote, ABA suggests that the NCUA clarify the status of jointly-owned accounts to permit either account holder to vote or require the signatures of both account holders on a single ballot. Eliminating the account type as a voting account is a draconian result and serves to highlight the need for the NCUA to clarify, rather than avoid, the issue.

Conclusion

While credit unions are technically not subject to the Act's provisions, the other regulators of depository institutions have applied the Act's principles that are consistent with FDICA and good corporate citizenship to these institutions, and the NCUA should do likewise.

In addition, ABA recommends various Federal Credit Union Bylaws modifications and disclosure enhancements which will directly benefit credit union members. If you have any questions, please contact the undersigned or Alison Touhey at 202-663-5034.

Sincerely,

John C. Rasmus