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NATIONAL CREDIT UNION ADMINISTRATION
Washington, D.C. 20456

February 21, 1989

Office of General Counsel

Alton P. Drain
General Manager
Mobay Employees Federal Credit Union
P.O. Box 500
New Martinsville, WV 26155

Re: Credit Union Policy Toward Bankrupt Members
(Your December 21, 1988, Letter)

Dear Mr. Drain:

You have asked our opinion as to whether a member may be denied a loan based on whether the member has filed for bankruptcy, even if the bankruptcy did not involve your Federal credit union. Neither the Federal Credit Union Act nor the National Credit Union Administration's (NCUA) Rules and Regulations prohibit such denial. You should, however, contact local counsel to determine if such a policy violates the Bankruptcy Act or any other applicable law.

The NCUA has consistently held that a member's fundamental rights in a Federal credit union (FCU) are to hold a share account and to vote at annual and special meetings. An FCU cannot withhold these rights without a formal expulsion. An FCU may be limited in what services are denied a bankrupt member by contractual agreements and by state and Federal laws, including the Bankruptcy Act. Any bankruptcy policy adopted by your FCU should be specifically stated, either in board meeting minutes as a result of board resolution or in your FCU bylaws. If you wish to amend your bylaws to implement such a policy, you must submit a nonstandard bylaw to the NCUA Regional Office for approval.

4-2-89

Enclosed are several letters issued by this Office addressing an FCU's policy toward bankrupt members.

Sincerely,

Hattie M. Ulan

HATTIE M. ULAN
Acting Assistant General Counsel

RD:sg
Enclosures

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3600

NATIONAL CREDIT UNION ADMINISTRATION
Washington, D.C. 20456

November 23, 1988

Office of General Counsel

R.E. Miron, President
Greater New Orleans Federal Credit Union
P.O. Box 53311
New Orleans, LA 70153-3311

RE: Bankruptcy Policy (Your October 13, 1988, Letter)

Dear Mr. Miron:

You asked if a Federal credit union ("FCU") can adopt a bylaw that would deny FCU services to a member when any portion of a member's debt is discharged in bankruptcy. It is our opinion that an FCU can limit services to those that have caused a loss to the FCU due to bankruptcy. An FCU may not withhold the minimum statutory rights of membership -- maintaining a share account and voting at annual or special meetings -- without a formal expulsion. An FCU may also be limited by contractual agreements and by state and Federal laws, including the Bankruptcy Act.

Enclosed are several letters issued by this Office addressing the subject. If you wish to amend your FCU's bylaws with a policy on limitation of services to those that have caused a loss to the FCU through bankruptcy, you must submit the amendatory language to the NCUA Regional Office in Atlanta for approval.

Sincerely,

HATTIE M. ULAN
Acting Assistant General Counsel

HMU:sg

Enclosures

FCIA Vol. V, J. Bankruptcy

Hattie

NATIONAL CREDIT UNION ADMINISTRATION GC 07-24

WASHINGTON, D.C. 20456

GC/JJT:sj
3600

October 21, 1988

Mr. Walter M. Reaves, Jr.
P.O. Box 55
West, Texas 76691

Re: Permissibility of Eliminating FCU Services to Members in Bankruptcy (Your July 15, 1988 Letter)

Dear Mr. Reaves:

Federal credit union ("FCU") law permits an FCU to establish a policy to withhold FCU services from members who have defaulted on a loan or who have caused the FCU a loss through bankruptcy. However, an FCU may not withhold the minimum statutory rights of membership -- maintaining a share account and voting at annual or special meetings -- without a formal expulsion. An FCU may also be limited by contractual agreements and by state and Federal laws, including the Bankruptcy Act.

Background

FCU extended a loan to a member. The loan was secured by an automobile and a share certificate issued by FCU to the member's mother. Member filed for bankruptcy and is now making loan payments to FCU pursuant to a Chapter 13 bankruptcy plan. The bankruptcy court has reduced the amount of the payments and the interest rate on member's loan from FCU. FCU wants to stop paying dividends on the share certificate pledged as security for the loan.

Analysis

The "management" of an FCU resides in its board of directors, supervisory committee, and, where constituted, credit committee. 12 U.S.C. §1761. We are unaware of any provision in the FCU Act, NCUA's Rules and Regulations, or the FCU Bylaws which would prevent an FCU's management from establishing a policy of withholding FCU services (e.g., ATM services, credit cards, loans, and dividends) to members who

Vol V, J - Bankruptcy

have defaulted on a loan or whose bankruptcy has resulted in a loss to the FCU.

However, FCU law does preclude management from preventing a member from exercising the statutory rights of membership -- maintaining a share account and voting at annual and special meetings. These rights can only be taken through a formal expulsion. We are enclosing several previous opinions on this issue for your review. An FCU must also ensure that such a policy does not breach a share account, share certificate or other contractual agreement between FCU and a member, or violate state or Federal law, particularly the Bankruptcy Act. In the facts you presented, the agreement establishing the share certificate pledged by the mother and the pledge agreement may not provide for a reduction in dividends in event of default. Moreover, the reduction may not be permitted under an order from the Chapter 13 bankruptcy judge.

Sincerely,

TIMOTHY P. McCOLLUM
Assistant General Counsel

JT:sg

Enclosures

NATIONAL CREDIT UNION ADMINISTRATION
Washington, D.C. 20456

GC/TPM:esj
3600

August 22, 1988

Office of General Counsel

Mr. Thomas P. Munley
Vice-President
Chryco Newark Federal Credit Union
P.O. Box 8065
Newark, Delaware

Re: Expulsion of Members (Your May 20, 1988, Letter)

Dear Mr. Munley:

A Federal credit union ("FCU") board may not expel members from an institution for "nonparticipation" under Section 118(b) of the FCU Act [12 U.S.C. §1764(b)] simply because they have caused the credit union a loss. A member can be expelled for causing a loss only by a member vote under Section 118(a) [12 U.S.C. §1764(a)]. Of course, the FCU board may refuse to extend credit and take other reasonable actions against such persons.
Article XVI, Section 1 of the FCU Standard Byalaws states:

> [a] member may be expelled only in the manner provided by the [FCU] Act. Expulsion or withdrawal shall not operate to relieve a member of any liability to this credit union. All amounts paid in on shares by expelled or withdrawing members, prior to their expulsion or withdrawal, shall be paid to them in the order of their withdrawal or expulsion, but only as funds become available and only after deducting therefrom any amounts due from such members to this credit union.

Section 118 of the FCU Act [12 U.S.C. §1764] sets out two methods of expulsion of members. Section 118(a) states: "[e]xcept as provided in subsection (b) of this section, a member may be expelled by a two-thirds vote of the members of a Federal credit union present at a special meeting called for that purpose, but only after opportunity has been given him to be heard." There are no restrictions as to what reasons constitute cause for expelling a member under Section 118(a); a member can be expelled under this procedure simply for causing the institution a financial loss.

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VC III(A)(1) Meetings, Membership, Special Meeting

Section 118(b) provides:

> [t]he board of directors of a Federal credit union may, by a majority vote of a quorum of directors, adopt and enforce a policy with respect to expulsion from membership based on nonparticipation by a member in the affairs of the credit union. In establishing its policy, the board should consider a member's failure to vote in annual credit union elections or failure to purchase shares from, obtain a loan from, or lend to the Federal credit union. If such a policy is adopted, written notice of the policy as adopted and the effective date of such policy shall be mailed to each member of the credit union at the member's current address appearing on the records of the credit union not less than 30 days prior to the effective date of such policy. In addition, each new member shall be provided written notice of any such policy prior to or upon applying for membership.

A member's causing the FCU a loss would not fall within the statutory provision of "nonparticipation . . . in the affairs of the credit union." It is not akin to failing to vote, purchase shares, obtain a loan from or lend to an FCU. Therefore, an FCU board cannot use its Section 118(b) authority to expel a member based on losses suffered because of the member's actions.

Only Section 118(a), which permits expulsion for any reason, provides authority for an FCU to expel a member based on losses he or she may have caused the FCU.

Sincerely,

TIMOTHY P. McCOLLUM
Assistant General Counsel

TPM:sg

NATIONAL CREDIT UNION ADMINISTRATION
Washington, D.C. 20456

2/11/86

Office of General Counsel

Bruce D. Foreman, Esq.
Melman, Gekas, Nicholas &
Lieberman
3207 North Front Street
Harrisburg, PA 17108-0902

Dear Mr. Foreman:

This responds to your letter of January 22, 1986, concerning the issue of termination or expulsion of Federal credit union (FCU) members. Specifically, you ask whether an FCU may adopt a written policy providing for expulsion where the member has caused financial loss to the credit union by failing to repay debts or other obligations or by discharging the same in bankruptcy or where the member disrupts the operation of the credit union with respect to conduct towards the credit union's officers or employees.

Article XVI, Section 1 of the FCU Bylaws states that a member may be expelled only in the manner provided in the FCU Act. As you have stated in your letter, Section 118 of the FCU Act, 12 U.S.C. §1764 addresses expulsion of members. Two methods of expulsion are set out in Section 118.

Pursuant to Section 118(a), a member may be expelled by a two-thirds vote of the members present at a special meeting called for that purpose, but not before the member to be expelled is given an opportunity to be heard. There are no restrictions as to what reasons constitute cause for expelling a member under Section 118(a).

Section 118(b), on the other hand, provides that an FCU may adopt an expulsion policy based on a member's "nonparticipation" in the affairs of the credit union. A member's failure to vote in annual credit union elections or failure to purchase shares from, obtain a loan from, or lend to the FCU are examples, provided in the Act, of what should be considered in formulating a nonparticipation policy. Under this method of expulsion, a special meeting need not be called but the policy must be reduced to a written form and mailed to each member of the credit union.

As seen from the above, it is reasonably clear that losses sustained by an FCU due to a member's discharged debts would not fall within the statutory provision of "nonparticipation. . . in the affairs of the credit union." Therefore, an FCU cannot adopt a written policy of expelling members based on losses suffered from discharged debts pursuant to the authority in Section 118(b). However, Section 118(a), which permits expulsion for any reason, would provide the authority for an FCU to expell a member based on losses he or she may have caused the FCU to suffer from discharged debts.

In addition to the ultimate sanction of expulsion, FCU's have various options available to address problems, injuries, or losses which the FCU incurs as a result of actions by certain members. An FCU's board of directors has the flexibility to fashion a whole host of policies which may be effective in dealing with the problems. An FCU is not precluded, under the FCU Act or NCUA Rules and Regulations from implementing a policy that denies access to virtually every credit union service (e.g., ATM services, credit cards, loans (assuming the policy is not violative of Regulation B or the Equal Credit Opportunity Act), preauthorized transfers, etc.), to anyone whose bankruptcy or loan default results in a loss to the credit union. However, the member must still be permitted to vote at all annual and special membership meetings, and to continue maintaining a deposit account (although, there is nothing which requires that the account still earn a dividend). I have enclosed copies of previous opinions on this issue for your convenience.

I hope we have been of assistance. If you have any further questions, please let me know.

Sincerely,

-S-

STEVEN R. BISKER
Assistant General Counsel

Enclosure

YG:cch

NATIONAL CREDIT UNION ADMINISTRATION
Washington, D.C. 20456

August 17, 1987

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3600

Office of General Counsel

Gerry Goodgion, Esq.
Executive Vice President and General Counsel
Connecticut Credit Union League, Inc.
P.O. Box 5001
Wallingford, CT 06492

Dear Mr. Goodgion:

This is in response to your letter concerning our opinion that dividends on regular share accounts of members who have defaulted on their loans or who have caused the FCU to suffer a loss because they entered bankruptcy may be reduced or otherwise eliminated.

It has been our stated opinion that a Federal credit union ("FCU") may have a policy to eliminate FCU services, including limiting or eliminating dividends on regular shares of a member who is in bankruptcy or who has defaulted on a loan, without violating the FCU Act or the National Credit Union Administration Rules and Regulations. However, the policy could not go so far as to preclude the member from voting at annual and special meetings.

Section 107(6) of the FCU Act (12 U.S.C. §1757(6)) states, in part, that:

> A Federal credit union . . . shall have power -
>
> * * *
>
> To receive from its members . . . (A) shares which may be issued at varying dividend rates; (B) share certificates which may be issued at varying dividend rates and maturities, and (C) share draft accounts authorized under Section 205(f); subject to the terms, rates and conditions as established by the board of directors, within limitations prescribed by the Board." (Emphasis added.)

Section 117 of the FCU Act (12 U.S.C. §1763) addresses dividends and states, in part, as follows:

> "At such intervals as the board of directors may authorize, and after provision of required reserves, the board of directors may declare a dividend to be paid at different rates on different types of shares, at different rates and maturity rates in the case of share certificates, and at different rates on different types of share draft accounts. . . ." (Emphasis added.)

In rendering our prior opinion in question here, we relied on the language highlighted above in Sections 107(6) and 117 of the FCU Act. We believe one can look to certain characteristics of the owners of shares when classifying "types of shares" for purposes of varying dividend rates. It is our opinion that an FCU can classify the shares of defaulters/bankrupts (debtors) differently from other shares and limit or completely eliminate dividends paid on such shares. Although it is our opinion that such treatment does not violate the FCU Act or NCUA Rules and Regulations, we do not render an opinion on any other applicable state or Federal laws.

I hope that we have been of assistance.

Sincerely,

STEVEN R. BISKER
Assistant General Counsel

HMU:sg

NATIONAL CREDIT UNION ADMINISTRATION
WASHINGTON, D.C. 20456

GC/RMK:dlp
3210
3500
3600
March 22, 1982

Board of Directors
Travis AFB Federal Credit Union
P.O. Box 1536
Travis AFB, California 94535

Dear Board Members:

We have been asked to review your proposed policy statement to deal with losses caused by member bankruptcies. This policy would have the effect of precluding members whose bankruptcy proceedings resulted in a loss to the credit union from being eligible for any credit union services until such time as the loss is made up by reaffirmation and full repayment.

It is assumed that a member whose bankruptcy brings him within the scope of this proposal will nevertheless not be denied the right to vote at annual and special membership meetings. Based on this assumption, it is our opinion that the policy statement you propose is not in conflict with either the Federal Credit Union Act or NCUA's attendant rules and regulations. With specific reference to the relation between a member's bankruptcy and his subsequent loan application, enclosed is an excerpt from the August, 1981 edition of the NCUA Review, which speaks directly to this point.

As you know, there is no basis upon which this Office can render an authoritative or binding opinion with respect to the application of the Federal Bankruptcy Code. However, you should be aware of the following. Section 525 of the Code (11 U.S.C. §525) protects a bankrupt from discriminatory treatment by any "governmental unit" that is based upon the fact of going through bankruptcy. The Code does not address discrimination by private parties. The legislative history of this section makes clear, however, that its prohibition is not intended to be exhaustive. It is intended to permit further development to prohibit actions by ". . . other organizations that can seriously affect the debtor's livelihood or fresh start, such as exclusion from a [labor] union . . . ." House Judiciary Committee Report No. 95-595, p. 367. Case law construing this provision is scarce, but we have found two cases that apply the ban on discrimination to state colleges and universities that had refused to provide transcripts to any graduate whose unpaid student loan was discharged in bankruptcy. Lee v. Bd. of Higher Education in City of New York, D.C. N.Y. 1979, 1 B.R. 781; Matter of Heath, Bkrtcy. Ill. 1980, 3 B.R. 351. I make note of this essentially for your information and suggest to you that it may bear further research by your own retained counsel. I would also simply point out that section 524 of the Code (11 U.S.C. §524) provides that no reaffirmation

agreement concerning a dischargeable debt is enforceable against the debtor unless the criteria set forth at subsection (c) of 524 have been met.

I hope this letter proves of value to you.

Sincerely,

JOHN L. OSTBY
General Counsel

By: JAMES J. ENGEL
Assistant General Counsel

Enclosure