

A Guide for Michigan State-Chartered Credit Union Directors

Introduction

Service as a credit union director can be a rewarding experience. Responsible, competent directors are crucial to the success of a credit union and hold positions of trust and honor.

The credit union industry is constantly challenged by a changing marketplace and as a result, directors must be proactive, dedicated, and attentive to the performance of their institution. Directors play a key oversight role in assuring compliance with the laws and regulations impacting credit unions, as well as the quality of products and services provided to the membership.

Credit union directors face high levels of scrutiny by the media, government, members and others in performing their duties. Directors must act carefully and prudently to protect their own individual liability and to ensure the credit union is operated efficiently and in accordance with applicable laws and regulations.

This guide was developed to answer basic questions you may have as a board member of a state-chartered credit union in Michigan and provide resources for further information. This publication is not intended to replace legal counsel. If you have specific concerns or questions regarding the responsibilities and liabilities of this role, you should contact an attorney.

Whether you're newly elected or a more seasoned credit union director, I applaud you for your willingness to volunteer. You play a pivotal role in ensuring that safe and sound financial services are provided to the members you represent. I hope this publication assists in your understanding of that role and the responsibilities of this very important endeavor.

What is my role as a board member?

Board members are individuals elected to represent and protect the interests of the members. The board is comprised of those individuals and collectively sets the vision and governs the credit union's overall activity. There is an important distinction between the individual opinions of each director and the pronouncements of the board. While individual directors are responsible to bring their attitudes and experience to discussions on matters before the board, individually they hold no authority other than the right to vote on those matters. Authority to govern the affairs of the credit union rests with the board collectively and is communicated only through its pronouncements (called board resolutions) properly moved and approved by a quorum (or majority) of the directors. Despite differences of opinion expressed during the approval process, individual directors must unequivocally support board decisions and ensure the board speaks with one voice even if their vote on a particular issue was of the dissenting opinion.

What are the individual responsibilities of a board member?

The board of directors is ultimately responsible for the conduct of the credit union's affairs. The board controls the credit union's direction and determines how it will operate. A board should hire capable management to ensure board-adopted policies and strategic plans are fully implemented and followed. While day-to-day operations are generally delegated to the CEO/management, the board is responsible for, and must assure through internal reporting and controls, that operations are carried out in compliance with applicable laws and regulations and consistent with safe and sound practices. The board monitors the credit union's overall operations and ensures management can meet the challenges created by growth, increased competition, and a changing marketplace.

Individual directors must become educated in the business of the credit union operations in order to effectively serve. Professional development and training are strongly encouraged. The managing officers of the credit union must be supported and supervised by directors who are thoroughly familiar with the credit union's affairs and who will take an active part in making policies and decisions. Directors should not be reliant on operational management to interpret financial data or other information received. Board members must be independent and able to question management about issues they do not understand or that are unclear. This helps to keep the credit union progressive, sound, and profitable.

Generally speaking:

- Directors should thoroughly understand their duties and responsibilities under the Michigan Credit Union Act (MCUA), their credit union's bylaws, common law and applicable regulations. Directors must take a pro-active approach in learning how to become competent in all areas necessary to effectively serve.
- Directors should have a genuine interest in their office, attend meetings regularly, and keep well informed about the affairs of their credit union and the credit union industry at all times.
- Directors should give undivided loyalty to their office and not engage in interests adverse to the credit union.
- Directors should possess the integrity to not use their office for personal benefits through information gained by virtue of their position.
- Directors should be capable of retaining confidences, as required under the MCUA, and refrain from divulging confidential information gained through their position.
- The director must be capable of evaluating facts, and free from prejudices or personal interest, in reaching sound, independent decisions.
- Directors should not lose sight of their primary responsibility, which is to protect the depositors who have placed their trust in them.

What is the purpose of and authority for regulatory examinations?

As the chartering agency, the Office of Credit Unions (OCU), within the Department of Insurance and Financial Services, is responsible to ensure the overall safety and soundness of the credit union industry within Michigan. In that capacity, the MCUA outlines specific responsibilities of the DIFS Director (previously titled the Commissioner of the Office of Financial and Insurance Services) and his/her agents.

These include requirements under Section 207 of the MCUA that a safety and soundness examination be conducted in each Michigan state-chartered credit union no less frequently than every 18 months. An OCU examination evaluates credit union overall inherent risk profile, adequacy of risk management and related appropriateness of capital earnings performance, and does not meet the audit requirements found in Section 344 of the MCUA. An audit is conducted to independently verify to the Board and membership that financial statements correctly and fairly represent the condition of the credit union.

All Michigan credit unions are required to maintain federal deposit insurance under Section 387 of the MCUA. The National Credit Union Administration (NCUA) is the federal agency responsible for providing deposit insurance and has promulgated rules which outline requirements for credit unions to maintain that insurance. Under those rules, NCUA can perform a review to assess the level of risk the credit union presents to the National Credit Union Share Insurance Fund (NCUSIF), the fund which ultimately underwrites the deposit insurance.

OCU and the NCUA perform examinations to assess the overall safety and soundness of the institution and the likelihood of losses to the NCUSIF. The findings of each examination are communicated to the DIFS Director and the NCUA Regional Director. Just as importantly, the results are submitted in a formal report to the directors of the credit union to ensure they are fully aware of the issues, including the level of regulatory concerns noted at their credit union. This information is presented in part to ensure the board has information necessary to reasonably fulfill their duties.

What is the board of directors' role in the examination process?

The board of directors should be involved in communications with their examiner and must review the report of examination to obtain an assessment of the credit union's financial and operating condition. The report of examination addresses the credit union's safety and soundness, quantity of risk, quality of risk management, and the overall level of supervisory concern. Directors should thoroughly understand weaknesses and adverse trends identified during an examination and the actions management plans to take or has already taken to address those weaknesses. The board must ensure supervisory concerns noted during examinations are corrected. The board may request to meet with OCU officials or examination staff at anytime to discuss examination findings or the current condition of the credit union.

What are the legal liabilities of the board of directors?

Director liability is based on holding a position of trust and the related duty to represent the membership's interests and carry out duties prescribed by statute and regulation. This responsibility, also referred to as fiduciary duty, is outlined by the credit union's bylaws and the courts.

The fiduciary duties of the board are defined by the courts through common law and fall within the following fundamental categories: the duty of care, the duty of loyalty, and the duty of candor or disclosure. The fiduciary and statutory duties for Michigan state-chartered credit union directors may be generally described as follows:

Duty of Care: This duty is a common law standard that holds directors to that degree of care which ordinarily prudent and diligent individuals would exercise in handling the affairs of others under similar circumstances. This means that directors must participate actively and to the best of their ability through the work of the board in order to assure themselves that all financial arrangements are safe, that all employees operate in a legal and ethical manner, and that all activities are within the law and regulations imposed on the credit union.

Duty of Loyalty: This is a general responsibility that prohibits directors from using their position of trust to further their personal interests above those of the credit union. It can include anything from respecting the confidentiality of information received to transacting their personal business with the credit union at arm's length. This does not mean that directors may not conduct business with the credit union. However, directors must disclose any personal interest in matters before the board, and if necessary, abstain from the related discussion and vote.

Duty of Candor or Disclosure: The duty of candor or disclosure requires directors to provide full and open disclosure of all facts and circumstances which may impact the board's deliberations on matters under consideration. It can include disclosure of direct and indirect business and personal relationships with individuals seeking to do business with the institution as prospective members, borrowers, or vendors.

Statutory and Regulatory Liability: Credit unions are subject to a framework of state and federal statutes. For Michigan state-chartered credit unions, relevant regulations include the MCUA, the insurance provisions of the NCUA Rules and Regulations, and a host of consumer protection, anti-money laundering and other regulations from both federal and state authorities. A director who fails to comply with applicable regulations, has engaged or participated in any unsafe or unsound practice in connection with the credit union, has committed or engaged in any act, omission, or practice that constitutes a breach of fiduciary duty of that person, and causes the credit union financial loss or other damage or that jeopardizes the interest of its members and depositors, could be subject to administrative remedies including removal from office and/or monetary fines. Major regulations impacting credit unions including web site addresses can be found on the OCU website at www.michigan.gov/creditunion.

Protection for directors against claims of negligence in performance of their duties can be afforded by the "business judgment rule" and appropriate indemnification insurance.

The business judgment rule requires directors to act as prudent and diligent business persons when selecting, monitoring and evaluating management; when establishing business policies and procedures; when monitoring and assessing business operations; and when establishing and monitoring adherence to policies required by law, regulation, and principles of safety and soundness. The rule guards against claims of negligence in the performance of duties, even if their decisions were wrong, as long as the behavior was guided by the good faith, objective and disinterested business judgment of the directors. Appropriate levels of due diligence are required when investigating new products, services or investments, or before entering into contractual relationships with third parties. This requires appropriate documentation to support conclusions by the directorate in performance of their duties.

A certain amount of protection against individual director liability can be obtained through the purchase of indemnification and director and officer liability insurance. Directors should be familiar with any insurance provided by the credit union.

What are the MCUA qualifications to serve on the board of directors?

Section 341(8) of the MCUA requires each director or committee member that has a significant influence over the ongoing operations of the domestic credit union to meet the following requirements:

- a. Be a member in good standing according to reasonable criteria established by the board.
- b. Be an acceptable bonding risk by a bonding company licensed to do business in Michigan.
- c. Has not been removed from a position at a financial institution by a federal regulator, another state regulator or a court of competent jurisdiction.

- d. Has not been removed by the Director (Commissioner) at a Michigan institution pursuant to the enforcement powers of the MCUA.
- e. Has not been convicted of a crime involving dishonesty or breach of trust within the past 20 years.
- f. Has not been habitually negligent in paying his or her financial obligations as determined by criteria reasonably established by the board or has not made, cosigned, endorsed or guaranteed a loan delinquent over 2 months as outlined under Section 342(8) of the MCUA and requiring automatic removal from the position.
- g. Has not been convicted by a court of competent jurisdiction of a violation or found in violation by a court of any law of this state enforced or administered by the Director (Commissioner).

Failure to meet any one of these requirements automatically makes the individual ineligible to serve and the office is deemed vacant.

Directors are elected at the annual meeting of the membership, unless appointed due to a vacancy. A director, when elected or appointed, shall take and subscribe to an oath that he or she will diligently and honestly perform the duties of the office and will not knowingly violate, or permit to be violated, any provisions of the MCUA.

How long is a director's term and how often does the board meet?

Under the standard bylaws, a regular term of office is typically three years. The board must meet at least 6 times in each calendar year and at least every other month. The board shall meet in person or by means of electronic communication devices that enable all participants in a meeting to effectively communicate with each other.

Is the director entitled to compensation?

Credit union directors serve as volunteers. An individual elected or appointed to serve as a director of a credit union is prohibited from receiving compensation for his or her service as a board member as outlined in Section 342(7) of the MCUA. However, the credit union may provide reasonable life, health, accident, disability, or similar insurance protection, and can reimburse board members for legitimate expenses incurred while conducting credit union business. Reimbursement for an official's actual lost wages when conducting credit union business would also be allowable.

Where can additional information be found about a credit union's board of directors?

Specific responsibilities of the board are further prescribed by the MCUA, each credit union's bylaws, and OCU Rules, Bulletins, and Letters. Each director should be familiar with these items which are available through your credit union and are also found on the OCU website at www.michigan.gov/creditunion. Regulations and agency pronouncements relating to share insurance requirements of the NCUA can be found at the NCUA website at www.ncua.gov. Contact information for DIFS and the NCUA can also be found on those websites. Directors should feel free to contact either regulator with specific questions and/or comments relating to the regulatory environment or the examination process.

If you have any questions regarding your duties and responsibilities or the MCUA, please contact the Office of Credit Unions.

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