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BY FAX AND E-MAIL

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, N.W.
Washington, D.C. 20552
Attn: No. 2006-29

Re: *Comments on Proposed Regulation Regarding Stock Benefit Plans in Mutual-to-Stock Conversions and Mutual Holding Company Structures; OTS No. 2006-29*

Dear Sir or Madam:

We appreciate the opportunity to submit comments on the Office of Thrift Supervision's (the "OTS") proposed regulation regarding "Stock Benefit Plans in Mutual-to-Stock Conversions and Mutual Holding Company Structures" ("Proposed Regulation") published in the *Federal Register* on July 20, 2006.[1] We are submitting these comments on behalf of a group of five (5) private institutional investment managers (the "Investors") with over $33.5 billion collectively in assets under their management. All of the Investors have made significant investments either in mutual holding companies ("MHCs"), publicly-traded federal savings associations ("Thrifts"), or other types of financial institutions.

We are writing to express the Investors' opposition to certain changes contained in the Proposed Regulation. In particular, the Investors are strongly opposed to the removal of the requirement that a majority of the minority (disinterested) shareholders approve any stock benefit plan in certain MHC structures. If the Proposed Regulation is implemented, it will permit the shares owned by a MHC, one year after conversion, to vote for the stock benefit plans for officers and directors of the MHC's subsidiary thrift. As a result of their existing investments, the Investors are in an excellent position to provide the OTS with insights about the potential impact of the Proposed Regulations on investors and minority shareholders of MHCs. Furthermore, the

[1] 71 Fed. Reg. 41179 (2006).

Investors have numerous other investments in other public and private companies and are keenly aware of the importance of good corporate governance.

The exact reasons for the Investors' opposition are discussed in more detail in Part II below. In short, the Proposed Regulation raises three primary concerns for the Investors. First, the Investors believe that the OTS rationale for the proposed change is inadequate especially in light of the more than ten-year precedent of the existing rule. Second, the Investors believe that the proposed change is inconsistent with the principles of responsible corporate governance and the recent focus by investors, shareholders and regulatory/self-regulatory authorities on good corporate governance and will adversely impact minority shareholders and investors in certain MHC structures. Third, the Investors believe that as a result of these two other matters, the Proposed Regulation, if adopted, may act as a disincentive to investment by third party investors in MHC structures, and thereby unnecessarily decrease the sources of capital available to Thrifts controlled by MHCs.

I. Overview of the Proposed Regulation

A. Background of the Existing Regulation

In 1994, the OTS substantially revised its conversion regulations to codify certain of its prior policies regarding the establishment of stock benefit plans in connection with conversions of thrifts from mutual-to-stock form.[2] The OTS intended these amendments to limit the benefits realized by management and a few selected individuals in such conversions, and give disinterested shareholders an opportunity to consider management performance before voting on a stock benefit plan.[3]

Currently, OTS regulations require that a majority of the outstanding minority shares approve any stock benefit plan and any management recognition plan. This requirement was established by the OTS in 1994 through the issuance of a final regulation after notice and comment by interested parties (the "1994 Final Regulation"). In the 1994 Final Regulation, the OTS noted that "while there are valid business reasons for thrifts to adopt stock benefit plans in order to attract and retain qualified management, these plans are now more appropriately implemented subsequent to conversion *and with shareholder approval*."[4] Of course, shareholder approval as contemplated by the 1994 Final Regulation means a majority of the minority (disinterested) shareholders, and not simply a majority of all interested and disinterested shareholders.

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2 59 Fed. Reg. 61247 (1994) (effective Jan. 1, 1995).

3 65 Fed. Reg. 43092, 43095 (2000).

4 59 Fed. Reg. 61247 (1994) (emphasis added).

The OTS further clarified this issue and its conversion regulations through the issuance of a letter by the Chief Counsel in 2004. The 2004 Letter required the approval of a stock benefit plan by a majority of all disinterested shareholders in a MHC structure.[5]

B. Overview of the Proposed Regulation

The Proposed Regulation contains two changes to the minority vote requirement. First, the OTS proposes to revise the provision to require a vote of the majority shareholders only during the first year after a minority stock issuance that was conducted in accordance with the mutual-to-stock conversion. Second, the OTS proposes to revise the provision to require approval (during the first year after a majority stock issuance) by a majority of the minority shareholders actually voting on the issue of adoption of the plan, rather then a majority of the outstanding minority shares. The first change presents the greatest concern to the Investors.

II. Investors' Opposition to the Proposed Regulation

We are writing to express the Investors' opposition to the Proposed Regulation and its expected adverse impact on minority shareholders in certain MHC structures. Specifically, the Investors believe that eliminating the requirement that a majority of the minority shareholders approve stock benefit plans would adversely impact minority shareholders and have an adverse impact on good corporate governance practices in many MHC structures. The Investors have three primary objections to the Proposed Regulation. First, the Investors believe that the rationale for these changes as noted by the OTS is inadequate. Second, the Investors believe that the proposed changes are inconsistent with responsible corporate governance – especially in light of the recent public focus on good corporate governance -- and adversely impact minority shareholders and investors in MHC structures without good cause. Finally, the Investors believe that as a result of these two other matters, the Proposed Regulation, if adopted, may act as a disincentive to investment by third party investors in MHC structures, and thereby unnecessarily decrease the sources of capital available to Thrifts controlled by MHCs.

A. Reversal of Existing OTS Precedent Not Supported

In the Proposed Regulation, the OTS offers two justifications for the changes to the voting requirements for the adoption of stock benefit plans. First, it suggests that the changes are necessary because the present regulation is "unduly restrictive." There is no analysis or supporting data included for this statement within the Proposed Regulation. Later, the OTS notes that the changes would "reduce the regulatory burden" on institutions, but there is no consideration or discussion of the potential harm resulting from this reduced burden.

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[5] OTS Chief Counsel Letter No. 2004-6 (Sept. 17, 2004) ("2004 Letter").

The Investors believe that a change in a regulation which has existed for over ten years should include more detailed rationale and evidence supporting such a change. The Investors and other shareholders have relied upon this existing regulation in making their investment decisions, and a reversal of this precedent without any detailed justification represents the adoption of the Proposed Regulation without the benefit of substantial evidence, which is contrary to accepted federal rulemaking standards and practices in administrative law and procedure. Thus, the OTS should specifically indicate what circumstances have changed since the 1994 Final Regulation and 2004 Letter that require the changes in the Proposed Regulation.

With respect to the OTS' claim that the existing regulation is "unduly restrictive", the Investors do not agree. Although the existing regulation imposes certain restrictions on Thrifts and MHCs, the Investors do not believe that such restrictions rise to the level of being "unduly" restrictive. In fact, institutions have managed to effectively operate within this existing regulatory framework for over ten years. Even if the OTS had offered support demonstrating that the existing regulation was unduly restrictive on the institutions, the OTS would need to consider whether such restrictiveness was warranted to prevent possible harm to minority shareholders. There is no such discussion in the Proposed Regulation.

The Investors recognize and commend the general interest of the OTS and other federal agencies in streamlining their existing regulations to reduce the burden on regulated institutions, and generally commend these efforts. There are instances, however, where these efforts must be carefully weighed against the potential harm that may follow from the removal of protections prescribed by an existing regulation that are designed to protect consumers, investors or other members of the public. The Investors believe that identified provisions in the Proposed Regulation present one such instance. Although the Investors agree that the Proposed Regulation in some manner would reduce the burden on MHCs, the Investors believe that any such benefits would be offset by a reduction in the protections afforded minority shareholders in MHC structures, including the Investors.

B. Corporate Governance

The OTS and other federal banking agencies have long endorsed sound corporate governance practices and encouraged all financial institutions to regularly review their existing operations and ensure that appropriate procedures are in place.[6] The enactment of the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley") and the corporate scandals which preceded it have increased the level of legislative, regulatory and public interest in the implementation of suitable measures that promote sound corporate governance. In many instances, companies, stock exchanges and regulators have required entities to put into place a number of additional policies and procedures

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[6] *See, e.g.*, OTS RB 37-5 "Oversight by the Board of Directors" (Nov. 2004); CEO Ltr No. 174 "Application of Recent Corporate Governance Initiatives to Non-public Banking Organizations" (May 2003).

to protect the rights of individual shareholders and to limit the power of management and other insiders. These procedures were designed in part to help build and maintain the value of the institution rather than simply creating wealth for the individuals managing the institution.

The Investors believe that if the Proposed Regulation takes effect as currently proposed, given that the MHC must control greater than 50% of the outstanding shares, it will give the MHC absolute control over all votes on stock benefit plans one year after a conversion. MHC officers and directors vote the MHC shares, and typically, these same individuals serve in the same capacity at the subsidiary thrift. Therefore, under the Proposed Regulation, management and directors, who are the financial beneficiaries of the stock benefit plans in question, would have the power to approve them without regard to the interests of the minority shareholders. Consequently, the Investors believe that the revised voting requirement would have no significance other than a legal formality and serve no legitimate corporate governance purpose. This exact concern was highlighted by the OTS in its 2004 Letter.[7]

In this era of increased scrutiny of corporate governance, including the recent investigations into management stock-option grant pricing at a number of public companies, the Investors find it particularly disconcerting that the OTS has proposed to reverse the 1994 Final Regulation, in which it determined that it was not appropriate for management to have absolute control in setting their own stock incentive compensation. The Investors are surprised that in the current environment, in which significant attention has been placed on the excesses of executive compensation, the OTS has decide to move toward a position of reduced corporate accountability and effectively reducing the rights of minority shareholders and other investors. Accordingly, the Investors strongly urge the OTS to reconsider the Proposed Regulation on the basis that it violates the underlying purposes of Sarbanes-Oxley and its requirements, undermines sound corporate governance, and undercuts the need for increased corporate transparency of publicly-traded companies.

C. Impact on Sources of Capital for MHCs

The Investors also believe that the Proposed Regulation may reduce the amount of new capital available to Thrifts controlled by certain MHCs and have an adverse effect on the financial condition of the industry. Other commenters have noted that the proposed change is necessary to attract and retain qualified management. Regardless of whether this point is true, the Investors do not believe that this change will encourage or attract new investors in MHC structures. Instead, the shift away from well established and strong corporate governance procedures will have the exact opposite effect and may encourage some investors and shareholders to invest their money elsewhere.

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7 2004 Letter at Page 2 ("Even though it otherwise exceeds the general charter requirements, requiring approval by a majority of the minority shares prevents the mutual holding company controlling the outcome of every such vote.").

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In conclusion, we appreciate the opportunity to submit comments on the Proposed Regulation on behalf of the Investors, and hope that the foregoing comments will be of assistance to the OTS and its staff in its preparation of a final regulation. We would welcome the opportunity to provide additional Investor comments or discuss any points in this letter. Thank you your for consideration of the foregoing.

Very truly yours,

Jeffrey P. Taft