

April 29, 2008

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

Sent via email

Re: Comments on Advanced Notice of Proposed Rulemaking for Parts 708a and 708b

Dear Ms. Rupp:

The Pennsylvania Credit Union Association (PCUA) and its member credit unions appreciate this opportunity to provide comments to the National Credit Union Administration (NCUA) regarding its advanced notice of proposed rulemaking related to transactions that significantly affect the rights of consumers who are members of credit unions (ANPR).

The PCUA is a statewide trade association that represents almost eighty-five percent (85%) of the approximate 593 credit unions located within the Commonwealth of Pennsylvania. To respond to this request for comments, the PCUA consulted with its Regulatory Review Committee (the Committee). This Committee consists of 12 credit union CEOs who lead the management teams of Pennsylvania federal and state-chartered credit unions. Members of the Committees represent credit unions of all asset sizes.

General Observations:

The underlying issues presented in the ANPR go to the very essence of one of the most important struggles faced by credit union management today, namely developing a growth strategy that allows for more and improved services for their members.

Even among our small group of credit union leaders, the differences in philosophy regarding the appropriateness of credit union mergers and conversions are evident. Everyone agrees that consumers and our local economies benefit from credit union services. But, the limitations and regulatory restraints on the charter make it ever increasingly difficult to reach the greatest number of consumers and small businesses who could benefit from credit union membership.

While we all agree that bigger is not necessarily better, most of us also agree that the bigger credit unions have more resources available to offer the types of products and services that consumers and small businesses need and want. While it is true that smaller credit unions often

provide some of the best levels of service, it is also true that the ongoing trend in the movement has been the merger of small credit unions into larger ones. And, when the larger ones become stifled by the limitations of their charters, they are faced with conversion options.

In particular, the current regulatory environment that requires credit unions to grow organically and the field of membership complexities and limitations increases the attractiveness of mergers and conversions into other types of financial institutions.

However, even with capital limitations and growth restrictions, credit unions continue to be identified by the media and financial industry analysts as the best deal for consumers. So, we raise the question why credit unions should be limited to serving only small sectors of the overall population? Shouldn't consumers have a choice? What could credit unions do for consumers and small businesses without field of membership restrictions?

We may be hyper-sensitive to this issue in Pennsylvania since we've been embroiled in a hotbed of litigation over our community charters, both federal and state. Our member credit unions are realistically only serving small sectors of the state but have been paying exorbitant litigation costs to protect their right to serve the fields of membership they have been legally authorized to serve. Why shouldn't consumers have the right to choose whether they want to obtain their financial services from for-profit or not-for-profit providers? And, why does that choice need to be limited?

We submit that there is enough room in the market place for both for-profit and not-for-profit financial providers. In the end, granting more opportunities to credit unions to service more people is a good thing for consumers and a good thing for our economy overall.

Management Duties/ Fiduciary Duty:

We agree with our many of our colleagues that the most important aspect of the ANPR is the NCUA's proposal to promulgated definitive standards and guidance regarding credit union board of directors' fiduciary responsibilities.

While we recognize that there may be some potential legal limitations to develop a standard fiduciary duty for officers and directors of *all* federally-insured credit unions, we encourage NCUA to do so. All of our Committee members agreed that inconsistency in the standard of care owed by officers and directors to the credit union and the members they serve is a problem. We also generally agree with NCUA's position that management decisions must be made in the best interests of the credit unions' members.

Pennsylvania law describes the fiduciary duty owed by directors of Pennsylvania for-profit and non-profit corporations as follows:

A director of a domestic corporation shall stand in a fiduciary relationship to the corporation and shall perform his duties as a director, including his duties as a member of any committee of the board upon which he may serve, in good faith, in a manner he reasonably believes to be in the best interests of the corporation and with such care, including reasonable inquiry, skill and diligence, as a person of ordinary prudence would use under similar circumstances. In performing his duties, a director shall be entitled to rely in good faith on information, opinions, reports or statements, including financial statements and other financial data....¹

Similarly, the responsibilities of officers of for-profit and nonprofit corporations are statutory set forth as follows:

Except as otherwise provided in the articles, an officer shall perform his duties as an officer in good faith, in a manner he reasonably believes to be in the best interests of the corporation and with such care, including reasonable inquiry, skill and diligence, as a person of ordinary prudence would use under similar circumstances. A person who so performs his duties shall not be liable by reason of having been an officer of the corporation.²

Under Pennsylvania law, the fiduciary obligation that a director owes to his/her corporation includes both a duty of care and a duty of loyalty.³ Once a fiduciary duty is imposed on a corporate director, one of the tests for liability for breach of a fiduciary duty is whether the director was unjustly enriched by his or her actions.⁴ A director may also breach his or her fiduciary duty by failing to disclose material facts⁵ or engaging in undisclosed self-dealings against a corporation's best interests and for his or her own financial benefit.⁶

Pennsylvania law generally provides the board of directors of a corporation with wide discretion to consider the interests of corporate stakeholders other than the shareholders, and expressly provides that maximizing shareholder value is not necessarily the primary duty of the board.⁷ Directors may, in considering the best interests of the corporation, consider the impact on a number of corporate stakeholders, including shareholders, employees, suppliers, customers, creditors of the corporation and communities in which the corporation is located. The board is

¹ 15 Pa. C.S.A. §§ 512(a)(for profit) and 5712(a)(nonprofit).

² 15 Pa. C.S.A. §§ 512(c)(for profit) and 5712(c)(nonprofit).

³ *In re Main, Inc.*, Bkrcty.E.D.Pa. 1999, 239 B.R. 281, supplemented 242 B.R. 574, affirmed in part, vacated in part, 2000 WL 1796417.

⁴ *In re Total Containment, Inc.*, Bkrcty.E.D.Pa. 2005, 335 B.R. 589.

⁵ *Resolution Trust Corp. v. Lutz*, E.D.Pa. 1996, 914 F.Supp. 1163.

⁶ *Westlake Plastic Co. v. O'Donnell*, E.D. Pa. 1998, 182 F.R.D. 165.

⁷ *See, Doing Public M&A Deals in Pennsylvania: Minesweeper Required*, William G. Lawlor, Peter D. Cripps, and Ian A. Hartman, Dechert LLP (September 7, 2005).

⁸ *Id.*

not required to deem any particular corporate interest as dominant and is allowed to determine the extent to which any interest should be factored into the equation for purposes of taking an action.⁸

We agree that the credit union board of directors should make their decisions based upon the best interests of the credit union's members and believe that this is not necessarily inconsistent with Pennsylvania state law. However, to the extent possible, we ask that NCUA specify what types of action and/or analysis by officers and directors in the types of transaction addressed in the ANPR support the notion that their fiduciary duties have been satisfied. It would also be helpful for NCUA to address the standard to be used in reviewing a credit union board's action. For example, is it the burden of the dissenting members of credit union to prove that the directors of the credit union did not act in good faith after reasonable investigation?

Most of our Committee members would like to see more guidance from NCUA in the area of fiduciary responsibility. One suggestion proffered by our group is to discharge the board's fiduciary responsibilities by providing an analysis of the decision in the articles of merger/conversion. The analysis would indicate what investigation was conducted, what information was considered and why the decision is in the best interest of the members (and any other credit union interest that the board considered).

Another request made by our group is for NCUA to establish more specific rules and provide greater clarification regarding board of director conflicts of interests and factors to be used in determining whether a conflict exists. It would also be helpful if NCUA indicated when it would be appropriate for a director to refrain from voting on a particular matter before the board due to a conflict of interest.

Mergers:

Some of our members feel that credit unions seeking merger partners should be required to publish their interest in some manner so that credit unions interested in pursuing a merger partner have an opportunity to engage in discussions with that credit union.

Others feel that publication of a credit union's interest in merging only heightens the possibility of insider enrichment and results in management shopping for the best payout.

Notwithstanding the two divergent views, there appears to be an interest in at least having a third party, maybe NCUA, broker information related to potential credit union merger candidates, especially for small and medium sized credit unions. We are not suggesting there be a general notice/publication requirement for credit unions that are proposing to merge with another credit union. However, for credit unions that want to seek out merger partners, NCUA may be in the best position to monitor and disseminate that information.

Member Right to Equity:

NCUA inquired whether credit unions merging or converting to another type of institution should be required to provide a merger/conversion dividend to their members as part of the process. If not, should the directors be required to consider the issue as part of its due diligence and then justify their decision to the membership?

Our committee members agreed that a merger dividend should not be required but that it makes sense for the board of directors to document why a decision was made not to return the equity to the member owners in merger or conversion proposals.

A requirement that a merger dividend be paid would certainly dissuade, if not eliminate, mergers of credit unions of similar sizes. In those cases, the capital of the merging credit union is often necessary to meet the regulatory capital requirements of the resulting credit union. However, when there is clearly excess capital, the decision of the directors not to return capital to the merging credit union members should be substantiated and documented in the plan of merger to be voted upon by the membership.

Communications to Members:

NCUA inquired whether it should issue a new rule on “hostile” mergers.

The consensus of our Committee members is that NCUA should not add any new rules that make it more difficult for credit unions to merge. However, our members do support a rule that provides guidelines for communicating with their members, as well as, members of other credit unions. Obviously, we agree that communications developed by the management or the board, on behalf of the credit union, should not be deceptive or misleading. In addition, there should be an equal and fair opportunity for all interested groups, whether they are member groups or management groups, to communicate with other members.

Bylaws:

Finally, we suggest that NCUA develop standard bylaws that can be adopted by the board of directors to establish the policy of the credit union regarding the types of transactions addressed in the ANPR. For example, under Pennsylvania state law, directors may adopt bylaws that dissuade third parties from initiating hostile takeover attempts of the corporation.

A credit union board of directors may want to adopt a standard bylaw provision that requires management to obtain a super majority vote of the members in order for the credit union to engage in a transaction that involves fundamental changes to the members’ ownership rights or the structure of the credit union, such as the transactions addressed in the ANPR. A super majority vote being defined as a requirement that the majority of members of the credit union must vote and that a majority of the members voting must approve the proposed transaction.

Ms. Mary F. Rupp
Secretary of the Board

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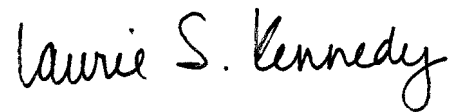
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Again, we are not proposing this as a requirement but rather as an option for the board's consideration.

Another standard bylaw may require that the members vote on whether a distribution of equity is required before a credit union converts to another type of financial institution, including a mutual savings bank.

Thank you again for this opportunity to comment on behalf of Pennsylvania credit unions. Please feel free to contact me or any of the PCUA staff at 1-800-932-0661 if you have any questions or if you would like to discuss our comments.

Sincerely,

A handwritten signature in cursive script that reads "Laurie S. Kennedy".

Laurie S. Kennedy
Associate Counsel

LSK:llb

cc: Association Board
Regulatory Review Committee
State Advisory Committee
J. McCormack
R. Wargo
M. Dunn, CUNA