From: Mary Sroufe (WCUL) [mailto:msroufe@waleague.org]
Sent: Tuesday, April 29, 2008 5:15 PM
To: _Regulatory Comments
Subject: Washington Credit Union League Comments on Advanced Notice of Proposed Rulemaking for Parts 708a and 708b

April 29, 2008

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

Re: Washington Credit Union League comments on Advanced Notice of Proposed Rulemaking for Parts 708a and 708b on Mergers and Conversions from Credit Union Charter

Dear Ms. Rupp,

As the trade association for Washington's 132 state and federally chartered credit unions, who have a total of more than 2.4 million members, the League is pleased to have the opportunity to comment on the NCUA's advanced notice of proposed rulemaking on Parts 708a and 708b of the NCUA rules.

Of principle importance, while the issues outlined in this ANPR represent important policy decisions, the League would like to see the NCUA subordinate its regulatory promulgation efforts to efforts designed to communicate the importance of maintaining a separate credit union regulator and share insurance fund to both the administration and Congress as these issues are currently paramount.

The NCUA's duty to preserve the safety and soundness of America's credit unions is, of course, its primary focus. Part of ensuring credit unions remain safe and sound is providing

them with a regulatory climate in which they can thrive. Credit unions do best when they have a wide variety of options to them—they need flexibility. In the current economic downturn, credit unions need agility to respond to member needs quickly and effectively. Regulatory burdens only inhibit that agility, they do not aid it.

Overall, the League feels that credit unions are currently being inundated with new rules and regulations. These rules are coming from various sources—not just the NCUA. However, the NCUA's recent emphasis on rulemaking has left credit unions reeling. The recent rules pertaining to member access to records, bylaw enforcement, and charter conversions have all been burdensome. In order to thrive, Washington credit unions need a respite from new rules and regulations, especially if the new regulations do not result in a significantly improved credit union operating environment.

Credit Union Conversions to Non-MSB Financial Institutions
The NCUA asks whether it should issue rules governing credit union mergers or conversions into a financial institution other than a mutual savings bank (or credit union) charter. The NCUA points out that such a rule might encourage conversions of this type. While the League firmly believes that the credit union charter is the financial institution charter most beneficial to consumers, it is important to note that credit unions do have the right to convert, even when that conversion is politically charged. To date, the NCUA has handled these conversions on an ad hoc basis. It would be helpful to have rules that address conversions to a non- MSB charter. Rule following credit unions should be allowed to convert in an efficient simple manner and not be delayed by endless studies on the matter. Conversion to a non-MSB charter could also be fairer to members, as a stock- held organization could protect member rights by distributing shares of the organization appropriately.

If promulgated, such a rule would need to address the fair valuation of a member's equity in the credit union and how that equity would need to be distributed, which will undoubtedly prove controversial. Such a change would require clear communication to the members, and it would make sense to make communication requirements consistent with other conversion processes.

Director's Fiduciary Duties
The NCUA seeks comment on whether the NCUA should address the fiduciary duty directors owe to members in a regulation and whether the NCUA should establish a regulatory standard of care for directors to help ensure that they meet their fiduciary duty to members. The League questions whether this issue is within the scope of the NCUA's rulemaking authority, as this area of law is generally dictated by state and common law.

The NCUA's proposal assumes that a credit union's board of directors has a fiduciary duty to the members of the credit union rather than to the credit union itself. While the League recognizes that the NCUA has opined on this issue, we continue to disagree with the NCUA's analysis. In Washington, case law specifically refutes the NCUA's analysis and remains the only case law that the League is aware of that is on- point in the United States. The examples provided by the NCUA fail to convince us that a board has fiduciary duties to the individual members of the credit union rather than the credit union as an entity.

The NCUA should not issue a uniform standard of care or regulations on directory fiduciary duties. Fiduciary duty issues are a state statutory or common law issue. The NCUA highlights the fact that case law and state law can vary widely from state to state and can cause confusion and a lack of uniformity between credit unions. We would agree that a lack of uniformity can cause confusion, however the nature of separate state laws is a rather important feature of the United States legal system. It can cause confusion, but it can also lead to innovation. We disagree that a lack of uniformity is necessarily a bad and undesirable feature and would again urge the NCUA not to adopt rules in this area.

Voting
The NCUA asks whether the agency should consider promulgating rules regarding the record date for members voting on a conversion proposal. While we'd reiterate our prior contention that credit unions are currently overwhelmed with new regulatory requirements, clarifying this issue would be helpful. This doesn't appear to be a particularly time- sensitive issue, and it doesn't appear to be something that the NCUA needs to address promptly, however, it would be helpful to eventually address the issue.

Net Worth Ratios During Mergers
The NCUA asks whether it should issue rules that provide credit unions with guidance on how

to deal with unequal net worth ratios among merging credit unions. The NCUA asks whether merger dividends should be required when credit unions with unequal net worth ratios merge, or whether the board of directors at the merging credit unions should be allowed to come to its own conclusions and then justify that decision to its members.

The League agrees that a merger dividend can be an effective way of fairly distributing the high net worth held by a merging credit union among its loyal members. There are many factors to be considered during a merger, however, and requiring a merger dividend could unnecessarily complicated a merger. For example, a credit union with high net worth could also have risky investments and a history of higher collection losses. The League believes that the merging credit unions should carefully consider these factors, but does not believe the NCUA should require a merger dividend.

The League would not be opposed to guidance that better describes how a merger dividend can be distributed to members, however. For example, who should receive the dividend? Should persons who have been a member of the credit union for twenty years be accorded the same dividend as a person who has been a member for just twenty days? Should a member who obtains five services from the credit union be accorded the same dividend as a person who only uses one of the credit union's services? These are questions that can best be answered on an individual credit union- by- credit union basis, but guidance from the NCUA could provide thoughtful issues to be considered.

Communication to Members

The NCUA asks whether it should consider a regulatory provision that specifically prohibits communications from credit union officials that state or imply that the NCUA has endorsed a charter change transaction or accompanying credit union materials. The League agrees with the NCUA's focus on clear communication and member understanding when contemplating changes to the credit union's structure. The League sympathizes with the NCUA's concern over the perception that a charter change is endorsed by the NCUA. It's easy to see how a perception of regulatory endorsement could occur since the NCUA often has an approval role in the conversion process. Providing credit unions with safeharbor language that clearly disclaims the NCUA's role in the decision- making process leading to the merger seems innocuous and would pose little burden to credit unions, unless the NCUA then began to dictate the size of the disclosure notice, disclosure notice placement, and the myriad details concerning the disclosure that never fail to create annoyance in other lending regulations.

The NCUA asks whether it should require converting credit unions to conduct research concerning whether services or branches would need to be closed in the future, and disclose these findings to members or whether the NCUA should issue a more general rule requiring the credit union to provide a full and fair disclosure to members.

The League agrees that the cessation of certain services or closing of branches are issues of great important to the members of a credit union, and that these issues should be disclosed to the members during a conversion. The League is somewhat concerned that changes in circumstances and business models could lead to litigation if a such a rule were issued. For example, a credit union choosing to convert might disclose that it has no plans to close any of its branches. Once converted, it may radically change its business model. In short, disclosures of this type only seem relevant for a very limited duration. The NCUA should seek to prevent the non- disclosure of information with an intent to mislead members, however, requiring a converting credit union to disclose its future service plans does not seem like it would be very effective. If the NCUA promulgates a rule on this issue, out of necessity, the NCUA should seek to issue a more general rule requiring full and fair disclosure.

The NCUA asks whether it should establish "hostile takeover" scenario communication standards that would have to be met as a condition of the NCUA's approval of a merger.

The NCUA accurately points out that even if it did establish standards, these standards would not be applicable to non- credit union entities. Part 740 already prohibits a federally insured credit union from using any advertising or making any representation that is inaccurate or deceptive or in any way misrepresents its services, contracts, or financial condition. The League believes that the standard established in Part 740 effectively addresses misleading communications. Further, there are litigation strategies a credit union could use to respond to a third party communicating inaccurate information to its members.

While the League believes that the standards already a part of the NCUA's rules are generally sufficient to address misleading information, the League would like to urge the NCUA to re-establish the pre- FIRREA standards that made it a federal offense to cause a reasonable person to question the future liquidity of a financial institution. Causing a reasonable person to question the liquidity of a federally insured financial institution (and hence possibly causing a run on the institution) is far more serious than mischaracterizing the management of a financial institution.

In short, while the League believes that communications from an entity to the members of a credit union urging a merger constitute terribly bad corporate manners, they should not be impermissible. If communications of this type are misrepresentations, both the maligned credit union and the NCUA already have remedies available.

Third-Party Communication to Members Standards

The NCUA should work to reestablish pre- FIRREA standards that make it impermissible for anyone to call into question the liquidity of a financial institution as this is far more serious than simply questioning the management of a financial institution or urging the consummation of a merger. The reinstatement of these regulatory principles seems especially necessary in this age of blogs and other unmoderated published material that is available to the national public. Institutional disparagement, either through negligence or actual malice, can have a very real effect on a financial institution's viability. It is vital to the integrity of our financial system that communication calling a financial institution's health into question is prohibited. With the passage of FIRREA these standards were lost, and we believe they would still be useful and valuable.

Voting Issues

The NCUA asks whether it should permit any credit union member to request a formal recount of any vote in which the margin of decision is very narrow. The League recognizes that the promulgation of such a rule would likely lead to a recount in most narrowly contested elections, and that a recount would add cost to a credit union's election process. However, the League also recognizes that narrowly contested elections are somewhat rare. As such, it seems reasonable to allow a person with standing to contest an election and ask for a recount. (Persons with standing would include the narrowly losing candidate or candidates.) It does not seem reasonable to allow any member to request a formal recount of the vote.

Much of the NCUA's concern with respect to voting appears to stem from a lack of confidentiality in voting. It's reasonable that members should be able to keep their vote confidential, and it's not unreasonable for the NCUA to require credit unions to respect an individual's confidentiality concerning voting. The League believes that NCUA already has the power it needs to address the voting concerns raised in the ANPR. As the regulator, the NCUA has the ability to oversee the election and ensure that the democratic process is followed. If the NCUA decides to address this issue with a rule, we would advocate a simple

standard that requires confidentiality and gives the NCUA enforcement authority over voting processes that fail to maintain confidentiality without addressing interim voting tallies, prohibitions against management obtaining lists of members who have voted, prohibiting credit union employees from distributing ballots, etc.

Thank you for your time and consideration. Please contact me if you have any questions or concerns.

Sincerely,

Mary Sroufe
Director of Regulatory Affairs
Washington Credit Union League

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