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April 30, 2008

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

RE: 12 CFR Parts 708a & 708b, 73 Fed. Reg. 5461-5466 (January 30, 2008); Mergers, Conversion From Credit Union Charter, and Account Insurance Termination

Dear Ms. Rupp:

The American Bankers Association[1] appreciates the opportunity to submit comments on the Advance Notice of Proposed Rulemaking (ANPR) of the National Credit Union Administration (NCUA) seeking comment on whether the NCUA should issue regulations governing six different types of merger and other charter changes. These proposed regulations address the following types of transactions:

- Merger of a federally insured credit union (FICU) into another FICU;
- Merger of a FICU into a privately insured credit union (PICU);
- Conversion of a federally-insured state credit union (FISCU) into a PICU;
- Conversion of a FICU to a mutual savings bank (MSB);
- Merger of a FICU into a financial institution other than an MSB; and
- Conversion of a FICU into a financial institution other than an MSB.

ABA offers its general assessment of the ANPR in addition to commenting on the specific questions raised by the ANPR.

General

To quote former President Ronald Reagan, "there you go again." The NCUA is once again attempting to use the administrative rulemaking process to block

[1] The American Bankers Association (ABA) brings together banks of all sizes and charters into one association. ABA works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members – the majority of which are banks with less than $125 million in assets – represent over 95 percent of the industry's $12.7 trillion assets and employ over 2 million men and women. Of FDIC mutually chartered institutions, both state and federally chartered, ABA represents the vast majority, including former credit unions.

NCUA-insured institutions, in some instances, from shedding their credit union charter. For certain transactions, the ANPR would render the credit union charter a veritable regulatory prison by erecting a formidable array of arbitrary barriers intended to prevent the ***free exit*** of an institution from the credit union charter. No banking regulator, at either the federal or state level, exhibits the NCUA's level of regulatory obstructionism on the issue of charter choice or even merger choice.

The stated purpose of the ANPR is the "protection of member interests in transactions where members have a great deal at stake because the transactions involve fundamental changes in their ownership or the structure of the credit union."[2] And again, "to make certain member interests are adequately protected including helping members understand the risks and rewards associated with these transactions."[3] The unstated theme that pervades the ANPR, however, is the NCUA's concern that five of the six charter actions at issue involve movement away from the National Credit Union Share Insurance Fund (NCUSIF). ABA respectfully suggests that this unstated concern is the true motivation behind the ANPR. For that reason, ABA encourages the NCUA to engage in an open and honest discussion of the issues that affect participation in the NCUSIF rather than attempting to "fix" the problem by erecting artificial barriers to charter choice and variations in regulators.

Specific Questions

The ANPR poses a number of questions to assist NCUA in its development of a regulatory proposal. The questions will be addressed in turn.

1. Case-by-case Approach or Rule?

The basic question posed by the NCUA is whether the six listed transactions require the promulgation of rules or whether they should continue to be addressed on a case-by-case basis. In general, the case-by-case approach is employed by most regulators, not just banking regulators, until sufficient experience is gained to promulgate a rule. Rulemaking has the benefit of transparency – everyone knows the process and the rules by which the agency will consider and act on applications. The creation of a set of stable rules regarding the approval of mergers and other transactions will benefit the industry

[2] 73 Fed. Reg. 5461, 5462 (Jan. 30, 2008).

[3] Id.

because it fosters predicable outcomes.[4] NCUA has before it enough of a body of experience in FICU and FICU mergers to promulgate rules, given the approximately 300 FICU and FICU mergers that occur annually– some encouraged by NCUA, others voluntary.

The newest twists – the importation of stock techniques into FICU mergers - requires a measured regulatory approach that provides both acquiring FICUs and target FICUs with a level playing field and equal tools. The appropriate regulatory role for the NCUA is referee, not facilitator or inhibitor. The development of a rule in this area needs to codify the experience, lessen the need for interpretative letters, and provide clear "rules of the road" for credit unions.

In this vein, one issue clearly in need of addressing by the NCUA is the practice of "share equalization," the process by which depositors at the target institution receive additional funds in an effort to equalize share values between the target and the acquiring credit union. This practice of paying target depositors to vote "yes" was employed by stock institutions seeking to acquire mutually chartered savings banks and savings and loan institutions in merger conversion transactions in the 1970s. It is problematic on two levels: the first is the diminution of resulting capital due to depositor payouts during a time of economic stress, and the second is the historic experience of excesses when depositors actively encouraged acquisitions in order to seek greater gains. The historic experience resulted in the imposition of a moratorium in the 1970s that in a manner continues today in the regulatory concern and discouragement of merger conversion transactions. Depositors, whether in a federally insured bank or credit union, logically will tend to support a transaction that involves the payment of additional monies above and beyond their deposit agreement and contracted rate of interest. Left to its logical evolution, the continued payment to depositors of "equalization" money will drive consolidation of the credit union industry. The challenge for the NCUA is balancing the ownership interests of depositors and the safe and sound operation of the industry.

2. Management Duties.

The ANPR stresses management's fiduciary duties in the listed transactions and basically implies that any change that results in an exit from the NCUSIF is a violation of those fiduciary duties to the depositors. While NCUA may believe that any movement from NCUSIF is unwise, only two of the six transactions results in depositors losing federal insurance for their deposits. The remaining

[4] This assumes that the rules do not change almost yearly as has been the case in FICU to MSB charter change.

transactions all result in depositors receiving either NCUSIF or FDIC protection. For these four transactions, the type of resulting charter can not be used as a basis for imposing additional fiduciary duties. As to the movement from federal insurance to private credit union insurance, ABA agrees that there is sufficient risk to require additional disclosures. If history is our teacher, it has demonstrated that there is greater risk associated with private deposit insurance as opposed to federal deposit insurance.

Further, with respect to each of the four transactions where federal deposit insurance remains with the resulting charter, there is no justification in law or fact for creating a unique standard for those transactions where the resulting entity is FDIC insured. It is simply not enough for the NCUA to state that a higher duty is required because the resulting institution will not be a credit union and the depositor will no longer be a credit union member. While the NCUA may strongly prefer that the resulting institution remain within its regulatory reach, NCUA has a regulatory obligation to administer its statutory duties fairly as it charters new credit unions and when it extinguishes that charter. The creation of a special set of fiduciary obligations that only apply in the instance where the entity becomes an MSB or other federally insured entity is beyond the NCUA's authority.

It also remains clear that NCUA does not recognize the ability of boards of directors to make informed business decisions. Again, when it seeks to substitute its judgment for the business judgment of the institution, the NCUA demonstrates its predisposition to mistrust deeply any board that would willingly choose to drop its credit union charter. This is a usurpation of the role of the board of directors in contravention of statute and common law. Every state has common law standards on the business judgment rule for its corporations and other forms of business. The U.S. Supreme Court has ruled that it is the state's business judgment doctrine that must be applied, not a fiat standard that regulators have attempted to bootstrap onto existing statute.[5]

3. Insider Enrichment

Much of the ANPR focuses on the potential for insider enrichment when a FICU becomes an MSB or another federally insured entity (*i.e.*, stock bank). Again, as ABA has stated numerous times before,[6] the federal and state banking agencies

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[5] Atherton v. FDIC, 519 U.S. 213, 117 S.Ct. 666, 136 L.Ed.2d 656 (1997).

[6] As ABA noted in its 2006 comment letter on FICU to MSB proposed changes, "Much of the NCUA's . . . changes attempt to reach the transaction not within the statutory ambit of the NCUA – conversion from the mutual to stock form of charter. NCUA justifies its actions through the

are experienced regulators who often deal with banks switching charters. It is handled in the ordinary course. Tried and proven rules, along with decades of experience, govern the process. There is predictability. There is a regulator in charge. The NCUA can rest assured that the other federal and state regulators are sufficiently capable of supervising the institution whatever charter is chosen and address appropriately the issues of insider enrichment.

It is curious that the ANPR does not focus equal attention on the transactions that result in depositors receiving only private insurance and where the potential for regulatory gaps is much higher. Surely if the goal of the rulemaking is "to make certain member interests are adequately protected including helping members understand the risks and rewards associated with these transactions," then the shift from federal to private insurance merits more regulatory attention.

4. Specific FICU to MSB Issues

The ANPR asks about a number of specific issues that have arisen during the process of a FICU merging or converting to an MSB. They will be addressed in turn.

Record Date. Because there is fluidity in the requirements for establishing when a depositor is a credit union member for purposes of determining eligibility to vote on the charter change, ABA supports NCUA establishing a clear set of rules. Depositors, NCUA, and management all benefit from understanding when *and how* a member receives voting eligibility. This would include clear rules on methods for removing dormant members from the membership rolls and verification of status as a current credit union member, including provision for periodic reviews of membership rolls. This would assist NCUA in its oversight of its field of membership requirements.

Member Right to Equity. As noted earlier, a member's right to equity in a merger transaction (merger dividend) has to be balanced with the safe and sound operation of the resulting entity and in cooperation with the resulting institution's regulator. In addition, the NCUA has to balance what may be unequal bargaining

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potential for personal gain by directors, management and employees. It is important to remember that the process by which a mutually chartered institution changes its form to a stock-owned institution is governed by a separate statute, with separate, fully promulgated regulations that have been tested for over 30 years. The process of mutual-to-stock conversion is subject to required disclosures, separate vote of the membership, an appraisal process, and detailed regulation and supervision. Yet the NCUA believes that it, not the regulator chosen by Congress, is uniquely competent in this process."

positions between larger and smaller institutions. This balancing is why the NCUA opinion letter ruling came to the conclusion that "per capita" dividends are impermissible and it highlights the delicate and complicated nature of the question. MSBs have case law that holds that depositors do not have a right to the capital of the institution, and ABA encourages the NCUA to consider that approach seriously.[7] The ANPR's cited transaction where a merger dividend was paid in an MSB context involved a highly unique set of circumstances that has not nor should not be cited as an accepted approach.

Improper or Misleading Communications to Members. The ANPR notes that because of NCUA's detailed rules governing disclosures to members, there have been instances where an implication arose that NCUA approved the transaction. This is simply the logical consequence of voluminous and exacting requirements. If NCUA is concerned that compliance with its regulations and requirements causes depositors to believe that NCUA has approved the communication and thereby the transaction, the solution is not to add *more* requirements. NCUA should recognize that the more it seeks to control the form and content of a communication via its overtly obstructionist regulatory requirements, the more likely the implication will be drawn.

In addition, NCUA is considering whether to require disclosure on the issue of moving or closing branches, particularly those branches in federal or state buildings where no rent is paid. This requirement would be yet one more disclosure in the litany of mandated disclosures that seek to prevent the credit union from choosing an alternative charter. Again, NCUA crafts its regulatory approach in a manner that is clearly biased against any other charter than a credit union charter. Such an approach is *ultra vires* and one that a credible regulator should not take.

Member Voting – Recounts and Interim Tallies. There are a number of questions posed by this issue, including methodology for recounts, credit union employees assisting in the voting process, and whether interim tallies are permissible. ABA urges NCUA to take a restrained view in this area. Credit unions pride themselves on taking excellent care of their depositors. That means that if it is a convenience to hand the teller the sealed ballot, or the customer service representative makes it easier for the depositor to vote, then the NCUA should encourage those activities. It is recognition of the culture of service. In the same vein, the number and volume of disclosures, as well as the frequency of

[7] Guitard v. Gorham Savings Bank, No. CIV.A.CV-00-326, 2002 WL 746106 (Me. Super., April 2, 2002).

formal canvasses, should be kept to a minimum in order not to inundate, confuse, or annoy depositors. That is not in keeping with the culture of service. It is also not in the culture of service to disclose the names of those who have not voted. Such disclosure is not allowed in elections for office or proxies, and is likely a violation of privacy.

On the issue of interim tallies, ABA suggests that NCUA recognize the natural curiosity of humans in wanting to check on voting progress. Indeed, voters are intrigued to watch election results during national, state, and local elections. ABA suggests that there are more pressing regulatory issues to be addressed than interim tallies.

Conclusion

For these reasons and others, ABA suggests that NCUA take a narrower approach to its rulemaking and respect the express limitations of the laws it is charged with administering. The NCUA's preoccupation with transactions that could result in institutions choosing to leave the credit union system for another regulator is neither appropriate nor supported.

Thank you for the opportunity to comment. If you have any questions regarding this comment letter, please feel free to contact me.

Sincerely,

C. Dawn Causey