Marvin C. Umholtz, President & CEO
Umholtz Strategic Planning & Consulting Services
1613 Easthill Ct NW Olympia, WA 98502
(360) 951-9111 marvin.umholtz@comcast.net

Sent via email: regcomments@ncua.gov

April 12, 2010

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

Re: Marvin Umholtz Comments on Notice of Proposed Rulemaking (Fiduciary Duties at Federal Credit Unions; Mergers and Conversions of Insured Credit Unions)

Dear Ms. Rupp:

I appreciate having the opportunity to present these comments to the members of the NCUA Board about the proposed rulemaking regarding duties of federal credit union directors, credit union conversion to mutual savings bank, merger of a credit union into a bank, credit union-to-credit union merger, and the termination of federal deposit insurance. The opinions in this comment letter represent my point of view and are not necessarily the views held by any of my clients or by any organization with which I may be affiliated.

It should be the job of all regulators, including the NCUA Board, to minimize regulatory obstacles, reduce compliance burdens, and facilitate legitimate business decisions. The NCUA Board would be doing a great service for the credit union industry by dropping plans to promulgate these complex and costly regulations governing Parts 701, 708a and 708b. The director's duties changes apply only to federal credit unions, but the changes are extremely damaging – adding to federal credit unions' reputation as having the riskiest governance rules, especially bylaws, in the financial services sector. The proposed merger and conversion rules make incrementally worse the already counterproductive existing rules that all federally insured credit unions must follow.

The NCUA Board should also streamline and simplify its current anachronistic and obstructionist regulations that impede credit union structure and governance changes. More NCUA time and resources should be spent monitoring the credit union industry's safety and soundness and mitigating the corporate credit union losses rather than dictating misguided notions of ideological correctness with these rules.

Umholtz NCUA Board Comment Letter Contents:

Overview of Proposed NCUA Board Regulations

According to the Board Action Memorandum (BAM) presented to the NCUA Board March 18, 2010, General Counsel Robert Fenner sought and received…"Board approval to issue proposed amendments to 12 C.F.R. Parts 701, 708a and 708b. The proposed amendments: (1) create new §701.4 to address fiduciary duties of FCU directors; (2) create a new subpart C of part 708a to address credit union to bank mergers; and (3) revise existing rules on charter and insurance conversions in parts 708a and 708b."

The BAM summary further explained, "Staff is proposing a number of changes designed to better protect credit union member rights and ownership interests. First, the new fiduciary duty rule in §701.4 requires FCU directors to carry out their duties in good faith, and have, or gain, an understanding of basic finance and accounting practices. Also, §701.4 prohibits FCUs from indemnifying its officials or employees for liability associated with misconduct that is grossly negligent, reckless, or willful in connection with a decision that affects the fundamental rights of members. Next, new subpart C of Part 708a establishes procedural and substantive requirements for converting a credit union to a bank through a merger. The new requirements would apply to both direct mergers and transactions where the credit union first converts to a mutual savings bank (MSB) and then merges with another bank without ever operating as a stand-alone MSB. Finally, the proposed amendments to Parts 708a and 708b revise existing rules to enhance the secrecy and integrity of the voting process in MSB and insurance conversions and require additional disclosures to members about the costs and effects of charter conversion."

The proposal also amends some of the existing regulatory procedures applicable to insured credit union mergers with other credit unions and the termination of federal deposit insurance. The new board of directors requirements would apply only to federally chartered credit unions, but the other provisions would apply to all federally insured credit unions. According to the regulatory proposal background information, the NCUA also anticipates future rulemaking on the conversion of insured credit unions into stock banks.

An overview of the NCUA Board's current complex and costly regulations governing conversion to the mutual savings bank charter is an addendum to this comment letter on pages 9 and 10.

Modernize, Repeal, and Rollback Existing NCUA Governance and Structural Change Rules

The NCUA Board should resist the temptation to over-regulate in the manner described in the proposed rules. The NCUA Board should instead modernize, repeal, and rollback the counterproductive structure and governance rules that are already in place. The NCUA Board should not support regulatory requirements that inappropriately obstruct credit union-to-credit union mergers, conversions to other financial institution charters, or conversions to alternative share insurance. Extending additional obstructionist rules to these strategic business choices is definitely not advised.

The NCUA has a long history of imposing its own narrow interpretation of what constitutes a "fully informed member" who is able to "consider the advantages and disadvantages" of a structural change affecting "member rights and ownership interests." Allowing credit union boards to develop a fair plan of merger or conversion is greatly preferred to a situation in which the NCUA Board substitutes its narrow judgment concerning what is best for each credit union's members. Each credit union should be able to choose any type of financial institution as a merger partner and/or convert to any type of financial institution charter or deposit insurance without inappropriate interference from NCUA.

If the NCUA Board pursues the public policy course suggested by this proposal, it will also have the net effect of making it easier for fringe groups to disrupt credit union mergers, conversions, and other structural changes that require membership votes. The NCUA's current governance regulations, including the federal credit union bylaws, would be laughable – if they weren't so dangerous.

As the past battles over credit union charter conversions have shown, it takes merely 750 FCU-member petition signatures, even at 3.4 million member Navy Federal Credit Union, to force a special membership meeting to remove the board of directors – and the anti-change activists know how to manipulate that flaw. These anti-structural change activists' tactics are clearly designed to force their narrow point of view on others, including on credit unions thousands of miles away from the activists' own communities.

Over the last several years, the NCUA Board has consistently adopted regulatory policies that disproportionably empower the outside activists and internal insurgents. The NCUA has also been ineffective in regulating the dissidents' defamatory outbursts and their intentional misinformation about charter conversions. Such disruption is certain to cause reputation risk for the credit union charter and expose the deposit insurance fund to more potential stress.

The NCUA Board is currently engaged in a regulatory process that will extend dissident insurgents' power to interfere in more credit unions' business decisions. The federal credit union bylaws already provide a mere handful of motivated members (customers) with the ability to hijack the credit union. The NCUA Board should take no additional steps that would further undermine the governance stability of a federally chartered or federally insured credit union.

Under the worst-case scenario, only those few structural changes that both the activists and the NCUA Board deem to be "ideologically-correct" will be allowed, and even those few transactions will be costly and complicated. With the adoption of these new proposed restrictions, the NCUA Board further handcuffs credit unions to the industry's systemic risk, interconnected capital structure, and potentially huge deposit insurance costs.

What credit unions need now are more strategic marketplace options, not the NCUA Board's micro-management and over-regulation. Creating additional obstructions to mergers, share insurance conversions, or charter changes without providing deposit insurance reforms, a solution for the corporate credit union legacy assets, access to alternative capital, or new growth and revenue opportunities, is a regulatory path leading to a dead end for the industry.

NCUA Board's Rules Based on Flawed Assumptions About Member Ownership

These NCUA rules that apply to mergers, charter conversions, and deposit insurance changes are based on flawed assumptions about the nature of a member's ownership of the credit union. The NCUA Board's continued insistence on the for-profit ownership interpretation applying to shared cooperative "ownership" places the credit union charter at increased risk for governance instability and severely restricts each credit union's strategic options.

Credit unions often provide members with great service and products, but hardly anyone joins a credit union so they can vote for the board of directors, attend the annual meeting, or cash in on their theoretical equity ownership by liquidating the credit union. Credit union members are more like federally insured financial institution depositors (customers) with limited voting privileges than they are like at-risk equity owners of for-profit companies.

Although credit union members (customers) have an individual pro-rata ownership interest (based upon deposit amounts) in their credit union's equity in the event of liquidation, their actual day-to-day relationship is more like that of a customer than like an owner of marketable stock. Since they are organized without capital stock, the applicability of laws designed for stock and other for-profit companies do not appropriately address the credit union relationship with its member (customer).

The NCUA Board members should read docket number 32858-5-II from the State of Washington Court of Appeals Division II filed 7/25/06. This Washington Appeals Court ruling in the case of Save Columbia CU Committee *et al*, Appellants v. Columbia Community Credit Union *et al*, Respondents confirms that credit union members are more like customers than stockholders. The Court said, "Columbia's members resemble depositors at a bank more than corporate shareholders." The issues addressed by that Court and its rulings are contrary to many provisions of these proposed NCUA governance, merger, and conversion rules – as well as to the NCUA's existing regulations. The Court's points should be carefully considered before the NCUA Board finalizes these proposed rules.

An individual's stock ownership in a for-profit company can be converted to cash at a time chosen by the stock owner/investor. This is very unlike a collectively-owned credit union in which an individual member typically receives a fair market value of zero for his or her intangible share of ownership when leaving the credit union.

When credit union members are allowed to cash out their share of the credit union's equity and take it with them to deposit in another financial institution down the street, then members will truly resemble stockholders. Until that becomes reality, a credit union member is merely a customer with a few voting privileges. NCUA's assumption as illustrated in this proposed rule that a credit union member has the same rights as a stockholder in a for-profit company is erroneous, bad public policy, and sure to be litigated and overturned in court.

The proposed rules appear premised upon the belief that a single credit union member's opinion on a merger, conversion, or other strategic structural choice is the functional equivalent to the business decision made by a credit union's duly elected leadership who are statutorily authorized to handle the vast majority of the credit union's operations and business affairs. Placing the individual member on the same level as the credit union's governing body is counterproductive if the agency wants its regulated and insured institutions to remain stable and viable.

According to the Federal Credit Union Act, the board of directors carries most of the responsibility for conducting the affairs of the credit unions. Statutory authorities granted to the membership are extremely limited in scope. There is no definitive statutory language that articulates an individual credit union member's specific right of marketable ownership of the institution or any part of the institution.

NCUA Board's History of Arbitrary and Capricious Rulemaking
Neither the existing or proposed NCUA merger and conversion rules represent good public policy. They make a credit union's choice to merge or covert unreasonably complex and unreasonably costly. They exceed the authority given the agency by statute and are wide-open to be challenged in court.

For example, in 2005, the NCUA invalidated the conversion vote at two Texas credit unions because of the way a single piece of paper was folded. The credit unions were forced to go to court where they prevailed (*Community Credit Union v. Nat'l Credit Union Administration, et al 2005*). The federal judge said NCUA was "arbitrary," "capricious," "silly," and "inept." Had the parties not settled, the judge would have invalidated NCUA's entire set of over-reaching conversion regulations.

The NCUA's existing conversion rules and the proposed new rules do not meet the statutory tests included in the Credit Union Membership Access Act of 1998 (CUMAA). When the U.S. Congress passed the CUMAA, it addressed congressional concerns that NCUA policy and regulations were hindering the ability of credit unions to change their charters and thereby exit the jurisdiction of the NCUA for a banking charter with insurance of accounts by the Federal Deposit Insurance Corporation (FDIC). In 1998, the Congress specifically repealed authority previously delegated to NCUA to approve charter conversions and provided that, on a going forward basis, such conversions were permissible without the prior approval of the NCUA Board. The 1998 Act further specified a specific voting process while limiting the role of the NCUA to administering and verifying the vote of the credit union members.

CUMAA also provided that the NCUA's rules for charter conversions by insured credit unions were to be consistent with rules promulgated by other federal regulators, including the Office of Thrift Supervision (OTS) and the Office of the Comptroller of the Currency (OCC) and are to be no more or less restrictive than that applicable to charter conversions by other financial institutions. The initial rules promulgated by the NCUA under the CUMAA met the congressional requirements.

However, as the number and asset size of credit unions seeking to convert began to increase, the NCUA adopted a series of additional regulations making it increasingly more difficult and expensive for credit unions to convert charters. The NCUA charter conversion rules are now twenty times longer, manifestly inconsistent with and indisputably more restrictive than the rules promulgated by other financial regulators, especially the OTS and OCC. The NCUA Board's conversion rules represent a less than subtle effort by the agency to subvert the will of the Congress as expressed in CUMAA.

Most of the problems in past credit union charter conversions, including those referenced by the NCUA Board in its notice of proposed rulemaking as the rationale for these rules, were the NCUA's own doing exacerbated by the agency's bureaucratic red tape and anti-conversion public relations tactics. The NCUA Board's restrictive anti-conversion rules impose a significant burden on a credit union by limiting its strategic options. The historical evidence suggests that the NCUA will continue being nitpicky and excessively bureaucratic in its handling of notices, member communications, and voting in mergers and conversions.

Imposition of NCUA-Approved Ideologically-Correct Standard of Care Misguided
It appears that the NCUA Board's intent is to exponentially enhance its punitive powers to dissuade board members from making any structural change decision that the NCUA Board deems ideologically-incorrect. "The proposal also amends the indemnification provisions of NCUA's rules to prohibit a federal credit union from indemnifying officials and employees for liability from misconduct that is grossly negligent, reckless, or willful in connection with a decision that affects the fundamental rights of members. NCUA is also proposing a change to NCUA's standard bylaw on indemnification to conform that bylaw with the proposed change to the rule on indemnification. The proposal makes a corresponding change to the standard federal corporate credit union bylaw on indemnification."

The NCUA Board admits that a standard of care already exists, but they plan to substitute their own version on federal credit unions in order to impose ideologically-correct behavior on boards of directors. "While the existence of fiduciary duties owed by directors to members is clear, neither the Act nor NCUA regulations provide specificity as to fiduciary duties and standards. Currently, an FCU's board must look to state statutory and case law to determine the scope of its fiduciary duties to members and the standard of care required as articulated by its state location. Statutory law and case law vary from jurisdiction to jurisdiction causing confusion for FCUs and a lack of uniformity between FCUs in different states. In fact, NCUA is particularly concerned about assertions that the members of a credit union do not own the credit union, or that the duties of the directors do not flow to the members, but, rather, flow in some amorphous way only to the institution."

This last sentence is the crux of the NCUA Board's misapplication of the credit union philosophical ideology to the statutory structure of the institution. The equity in the credit union is collectively owned, not individually owned and marketable. The duties of the board of directors do indeed flow to the institution and not to the members as individuals – or even collectively. What is in the fundamental best interests of one member might not be in the best interests of another. That's why each credit union board must make the determination on behalf of the collective membership by acting in the best interests of the institution as a whole and not each member as an individual.

The NCUA Board continued with its hubristic characterization of the situation. "Considering the unique interests, concerns, and structure of credit unions as financial cooperatives, NCUA believes having a uniform regulatory standard of care for FCUs may be useful to eliminate confusion and may make it easier for FCU boards to fulfill their duties to members. Accordingly, NCUA is now proposing a regulatory standard of care for directors that will help ensure they meet their fiduciary duties to their members, both in general and also when making decisions that affect the fundamental interests of members." The NCUA Board's self-aggrandizing rationale just doesn't hold water – and establishes an unsettling precedent.

At best, the NCUA Board's proposed preemptive standard of care for federal credit union directors is unnecessary. At worst it is indicative of the NCUA Board's intent to get directly involved in enforcing each credit union board's adherence to the NCUA Board's definition of ideologically-correct behavior. Based upon a convoluted chain of statutory citations to justify its meddling, the NCUA Board makes it abundantly clear that it intends to substitute its judgment as what is in the credit union members' "fundamental interests" rather than respect the judgment of thousands of duly-elected credit union boards of directors – or for that matter, the judgment of each individual member.

The proposed rules also blatantly undermine state laws on corporate governance. It appears that the NCUA Board is proposing this preemptive standard of care for federal credit unions for its own convenience – making it even easier for the agency to interject itself into an individual credit union's strategic structural change decisions. This correspondent would instead hope that the NCUA Board would conduct its affairs fairly and impartially, and avoid imposing this NCUA-sanctioned ideologically-correct standard of care on credit unions.

Proposed Rules Require Ideologically-Correct FCU Staff, Attorneys, Accountants, Advisors, and Consultants

This correspondent is also disturbed by the NCUA Board's proposed standard of care imposed in Part 701.4 regarding federal credit union staff and outside consultants. The fear is that the NCUA Board will again apply its own ideologically-correct expectations in defining who among the staff or outside consultants are reliable and competent. Given the NCUA Board's history as cheerleaders for the credit union charter, it seems unlikely that any staff, attorneys, accountants, advisors, or consultants that suggested merging with or converting to a non-credit union charter or changing deposit insurance would be deemed "competent and reliable."

According to NCUA, "Proposed paragraph (d)(1) permits a director to rely on one or more officers or employees of the Federal credit union who the director reasonably believes to be reliable and competent in the functions performed or the information, opinions, reports, or statements provided. In determining whether an officer or employee is reliable, the director would typically consider the individual's record for honesty, care, and ability in carrying out responsibilities which he or she undertakes. In determining whether an individual is competent, the director would normally consider the individual's background, education, experience and scope of responsibility within the credit union, the individual's familiarity and knowledge with respect to the subject matter, and the individual's technical skill."

The NCUA explanation continued, "Proposed paragraph (d)(2) permits reliance on legal counsel, independent public accountants, or other persons retained by the Federal credit union, but only as to matters involving skills or expertise the director reasonably believes are matters (i) within the particular person's professional or expert competence, and (ii) as to which the particular person merits confidence. A determination of competence involves an examination of factors similar to those discussed in connection with determining competence under paragraph (d)(1). Likewise, a determination that the potential advisor merits confidence includes an examination of both competence and reliability, including whether the individual may be subject to conflicts of interest or may have a vested interest in the outcome of any transaction under advisement. This paragraph covers not only lawyers and accountants, but also other potential external advisors with special experience and skills, such as investment bankers and management consultants."

Does the NCUA Board plan to maintain a secret and/or published "black list" of unacceptable ideologically-incorrect consultants and advisors? Will the NCUA Board preclude advisors that do not share its extremist views concerning credit union ownership and the members' fundamental interests? Is there even such a thing as a "neutral" staff member or advisor without a vested interest or stake in the outcome? It would appear that the NCUA Board is setting the stage for a high stakes game of ideologically-correct "gotcha."

CU-to-MSB Charter Conversion and CU-to-Bank Merger Costs Would Escalate

The proposed changes to Parts 708a and 708b represent the latest salvo in an ongoing process whereby the NCUA Board has sought to discourage credit unions from exercising strategic choices for structural change – most notably the conversion from the credit union charter to that of a mutual savings bank. These proposed rules apply many of the same regulatory hurdles – alarmist boxed disclosures, empowerment of dissident members, repetitive notices, to name just a few – to credit union-to-bank and credit union-to-credit union mergers. The proposed rules also include some changes that are merely annoying – like prohibiting interim vote tallies for conversions or mergers – but these changes still add new costs and further complicate the structural change process.

Perhaps the NCUA Board's most costly proposed requirements are the new disclosures and communications to members. As NCUA explained, "The proposal adds required disclosures about the estimated costs of conversion; the conversion's affect on the availability of facilities, including branches and ATMs; and the fact that NCUA neither approves nor disapproves of the proposed conversion…The credit union must disclose the total estimated cost of the conversion with separate line items for printing fees, postage fees, advertising, consulting and professional fees, legal fees, staff time, the cost of holding a special meeting, the cost of conducting the vote, and any other conversion-related expenses." This is essentially NCUA-required speculation about conversion costs. Like other disclosures, the NCUA Regional Director must approve or disapprove the content of this member communication – further raising doubts that NCUA will act in an even-handed manner rather than obstructing structural changes.

The new rules require that a potentially-costly merger value assessment be done in a credit union-to-bank merger. NCUA says, "The directors must conduct due diligence so as to determine that the concept of merging with a bank, and with the particular bank under consideration, is in the best interests of the credit union's members. As part of this due diligence, the directors must determine the merger value of the credit union, that is, the amount of money that a stock bank would pay in an arms-length transaction to purchase the credit union's assets and assume its liabilities and shares. The rule permits the credit union to obtain this valuation through either a public auction process or an independent appraisal process."

The NCUA Board's merger and conversion rules appear founded on the prejudiced premise that a credit union charter is the best federally insured depository institution charter and that no other charter choice can be made by a "fully informed" membership. It would be more appropriate for a federal regulatory and insuring agency like NCUA to demonstrate its support of the efforts of any federally insured depository institution to organize under the charter that bests suits its business plan and operating strategy. These NCUA rules will add more substance to the criticism that the agency is a cheerleader for the credit union industry rather than an even-handed safety and soundness regulator.

Proposed CU-to-CU Merger Rules a Disservice to the Industry

During any given year only a handful of credit unions will consider the option to convert to a mutual savings bank charter. Mergers with other types of financial institutions are even less common. Additionally, those state chartered credit unions that prefer state-authorized alternative deposit insurance remain limited in number.

However, hundreds of federally insured credit unions engage in credit union-to-credit union mergers each year and hundreds more consider mergers to be an important future strategic option for growth and/or survival. Applying new and complex rules to the credit union-to-credit union merger process will do a great disservice to the industry as well as to the individual consumer members it serves.

The NCUA Board's proposed rules impose new requirements and disclosures for credit union-to-credit union mergers in Part 708b. "The proposal amends subparagraph (a)(5) of this section to require additional information in the merger plan submitted to NCUA in cases where the merging credit union has a higher net worth ratio (NWR) than the continuing credit union. In these situations, the proposal would require the merger plan to discuss not only actual share adjustments, but an explanation of the factors used to establish the amount of the adjustment or to determine no adjustment is necessary. NCUA is proposing these additional disclosures because of the potential for unfair treatment of members of the credit union with higher net worth."

The NCUA continued, "One way to prevent loss of equity by members of a merging credit union that has a higher NWR than the continuing credit union is to compensate members of the merging credit union with a merger dividend, termed a share adjustment in Part 708b…Under the proposal, where a merging credit union has a significantly greater NWR than the continuing credit union, meaning in excess of 500 basis points greater, the required explanation must also include the factors considered in establishing the amount of the adjustment or in determining no adjustment is necessary."

There is nothing inherently wrong with distributing a special dividend in conjunction with a merger, but to establish that expectation based upon a flawed premise is not prudent. The members of a high net worth ratio credit union might prefer increased convenience (branches, online, etc.), a broader selection of products and services, or other tangible benefits rather than receiving a pro-rata distribution of "excess equity" based on deposit amounts. For that matter, the very absence of those post-merger benefits might be why the merging credit union had such a high NWR in the first place. The need for a share adjustment plan, especially its associated costs, might also serve as a deal killer that would make merging in small credit unions not worth the effort. The NCUA Board should be encouraging credit union-to-credit union mergers, not discouraging them.

Since NCUA must review and approve any merger plan involving a federally insured credit union, this correspondent doubts that the NCUA will approve any merger plan that it deems ideologically-incorrect. The NCUA Board is also setting the stage for any dissident member to hold the credit union merger hostage if dissatisfied with the amount of a share adjustment or the lack of one. Once again, the NCUA Board is making the flawed assumption that an individual member "owns" specific (rather than collectively-owned) equity in the credit union in circumstances other than liquidation.

As it applies to mergers, the NCUA Board should be a hands-off, arms-length regulator that does not force-feed its own concept of what is best for members or for the industry. NCUA's appropriate role in the merger process is a simple one: protect the safety and soundness of members' savings while staying out of the way of strategic business decisions made by individual credit unions.

Do Not Adopt the Complex and Costly Proposed Rules

Adding additional burdens to governance, mergers, and conversions is the last thing the credit union industry needs at this time. The NCUA Board seems singularly unwilling to act in a fair and impartial way, as befitting a regulator – and instead is establishing by decree an ideologically-correct interpretation of "member rights and ownership interests" that will have a chilling effect on strategic structural changes.

The proposed rules are based upon flawed concepts of member ownership of credit union equity and irresponsibly endow dissident members with the ability to derail structural changes that could benefit the institution and the vast majority of members. Despite attempts to justify NCUA's rationale to impose these over-reaching rules, by adopting these rules the NCUA Board will be making a bad situation worse.

Regardless of whether a credit union's leaders have plans to merge with another credit union or bank and/or convert charters or simply want to preserve these strategic options for the future, they should be particularly disappointed in the NCUA Board's regulatory over-reaching. These proposed and the existing complex rules will not stop a credit union that is determined to merge or convert, but the rules will certainly increase the cost of doing so. Attorneys and merger and/or conversion consultants will have the most to gain since they will be able to justify significantly higher fees once these NCUA Board proposed rules become final.

If you have any questions concerning these comments, please feel free to contact me for clarification or elaboration.

Sincerely,

Marvin C. Umholtz, President & CEO
Umholtz Strategic Planning & Consulting Services
1613 Easthill Ct NW
Olympia, WA 98502
(360) 951-9111 cell
marvin.umholtz@comcast.net

Marvin Umholtz is President & CEO of Umholtz Strategic Planning & Consulting Services based in Olympia, Washington south of Seattle. He is a 34-year credit union industry veteran who has held many leadership positions with credit union organizations and financial services industry vendors during those years. An accomplished speaker and former association executive, he candidly shares his credit union industry knowledge and insight with public policy makers, financial industry executives, and vendor companies. Umholtz also helps credit union boards and CEOs with strategic issues like growth, board governance, charter conversions, proactive mergers, voluntary liquidations, regulatory advocacy, and the growing conflict about the future role of credit unions in the financial services industry.

Addendum – Current NCUA Regulations:
Conversion to the Mutual Savings Bank Charter

"A credit Union, with the approval of its members, may convert to a mutual savings bank or a savings association that is in mutual form without the prior approval of the NCUA, subject to applicable law governing mutual savings banks and savings associations and the other requirements of this part." – National Credit Union Administration (NCUA) Regulations 12 C.F.R. Part 708a *et al* implementing 12 U.S.C. §1785(b)(2) of the United States Code that is contained in the Federal Credit Union Act.

1. **Notice to Members of Pending CU Board Vote on Conversion Proposal**. "No later than 30 days before a board of directors votes on a proposal to convert, it must publish a notice in a general circulation newspaper, or in multiple newspapers if necessary, serving all areas where the credit union has an office, branch, or service center."

2. **Posting of Notices in Lobby and on Website**. Notice posting in all credit union office lobbies and on the credit union's website are also required prior to the board's vote on the conversion proposal. The NCUA regulation specifies what must be in the notice. Member comments on the proposal are solicited and must be considered prior to action on the conversion proposal by the board of directors.

3. **Credit Union Board Majority Vote on Conversion Proposal**. "The conversion proposal may only be approved by an affirmative vote of a majority of board members who have determined the conversion is in the best interests of the members. If approved, the board of directors must set a date for a vote on the proposal by the members of the credit union."

4. **Notice to NCUA Regional Director**. "If a converting credit union's board of directors approves a proposal to convert, it must provide the Regional Director with notice of its intent to convert during the 90 calendar day period preceding the date of the membership vote on the conversion." The NCUA regulation specifies what must be included in the notice to the RD, including a description of the material features of the conversion as well as sample membership notices, the conversion vote ballot, and written materials intended to be distributed to members.

5. **Written Notices to Members of CU's Intent to Convert**. "The credit union must provide written notice of its intent to convert to each member who is eligible to vote on the conversion. The notice to members must be submitted 90 calendar days, 60 calendar days, and 30 calendar days before the date of the membership vote on the conversion."

6. **Conversion Ballot Distribution Limited to 30-Days Prior to Vote**. "A ballot must be included in the same envelope as the 30-day notice and only in the 30-day notice. A converting credit union may not distribute ballots with either the 90-day or 60-day notice, in any other written communications, or in person before the 30-day notice."

7. **Membership Vote Notice Requirements**. The NCUA regulations further outline the content of the membership vote notices including, among other things, the date, time, and place of the meeting to consider the conversion proposal. Members may vote at the special meeting or by submitting the written ballot. Significant other requirements must also be met.

8. **NCUA Requires Specific "Boxed Disclosures" to Membership**. "A converting credit union must provide the following disclosures in a clear and conspicuous fashion with the 90-, 60-, and 30-day notices it sends to its members regarding the conversion." The required disclosure must read: "**Important Regulatory Disclosure About Your Vote** The National Credit Union Administration, the federal government agency that supervises credit unions, requires [insert name of credit union] to provide the following disclosures: 1. LOSS OF CREDIT UNION MEMBERSHIP. A vote "FOR" the purpose of conversion means you want your credit union to

become a mutual savings bank. A vote “AGAINST” the proposed conversion means you want your credit union to remain a credit union. 2. RATES ON LOANS AND SAVINGS. If your credit union converts to a bank, you may experience changes in your loan and savings rates. Available historic data indicates that, for most loan products, credit unions on average charge lower rates than banks. For most savings products, credit unions on average pay higher rates than banks. 3. POTENTIAL PROFITS BY OFFICERS AND DIRECTORS. Conversion to a mutual savings bank is often the first step in a two-step process to convert to a stock-issuing bank or holding company structure. In such a scenario, the officers and directors of the institution often profit by obtaining stock in excess of that available to other members.”

9. **CU Must Distribute Individual Member’s Conversion Related Materials**. “A converting credit union must mail or e-mail a requesting member’s proper conversion-related materials to other members eligible to vote”…Any member or group of members in favor of or opposed to the conversion can request and pay for the credit union to distribute their comments and opinions to the credit union’s other members. The NCUA regulations provide some limits concerning the member communications.

10. **Member Comments on CU Website**. “If a credit union posts conversion-related information or material on its website, then it must simultaneously make a portion of its website available free of charge to its members to post and share their opinions on the conversion.”

11. **Membership Approval of a Proposal to Convert**. “A proposal for conversion approved by a board of directors requires approval by a majority of the members who vote on the proposal…The vote on the conversion proposal must be by secret ballot and conducted by an independent entity…The board of directors of the converting credit union must certify the results of the membership vote to the Regional Director within 10 calendar days after the vote is taken.” The NCUA regulation provides extensive guidelines outlining the agency’s expectations on how…“a converting credit union must conduct its member vote on conversion in a fair and legal manner.”

12. **NCUA Oversight of Methods and Procedures of Membership Vote**. “The Regional Director will review the methods by which the membership vote was taken and the procedures applicable to the membership vote. The Regional Director will determine: if the notices and other communications to members were accurate, not misleading, and timely; the membership vote was conducted in a fair and legal manner; and the credit union has otherwise complied with part 708a.” The NCUA regulations provide that the agency can disallow the vote and require a new vote.

13. **Other Regulator Oversight of Membership Vote**. “The federal or state regulatory agency that will have jurisdiction over the financial institution after conversion must verify the membership vote and may direct that a new vote be taken, if it disapproves of the methods by which the membership vote was taken or the procedures applicable to the membership vote.” Following the NCUA’s and the new regulator’s approvals of the conversion vote, the credit union has one year to complete the conversion or a new vote would be required by NCUA.

14. **Limit on Compensation of Officials**. “No director or senior management official of an insured credit union may receive any economic benefit in connection with the conversion of a credit union other than compensation and other benefits paid to directors or senior management officials of the converted institution in the ordinary course of business.”

15. **Voting Incentives Requirements**. “If a converting credit union offers an incentive to encourage members to participate in the vote, including a prize raffle, every reference to such incentive made by the credit union in a written communication to its members must also state that members are eligible for the incentive regardless of whether they vote for or against the conversion.”