



May 26, 2010

Mary Rupp, Secretary of the Board  
National Credit Union Administration  
1775 Duke Street  
Alexandria, Virginia 22314-3428  
Via Email: [regcomments@ncua.gov](mailto:regcomments@ncua.gov)

**Re: Comments On Proposed Regulations 12 CFR Parts 701, 708a, and 708b**

The National Center for Member Trust would like to thank NCUA for this opportunity to comment on the proposed regulations regarding Fiduciary Duties at Federal Credit Unions and Mergers and Conversions of Insured Credit Unions. The National Center for Member Trust (NCMT) is a non-profit organization, formed in 2006, that serves as resource for credit union members on credit union-to-bank conversions. More information about NCMT can be found on our website, [www.MemberTrust.org](http://www.MemberTrust.org).

As an organization that works with credit union member-owners on credit union-to-bank conversions and mergers, NCMT is acutely aware of some of the problems of these proposed rules seek to address. NCMT generally believes NCUA's suggested regulations would improve the conversion decision making process. In particular, NCUA's proposed regulations affirm that directors have a fiduciary responsibility to act in the best interests of the members, help to safeguard the integrity of the election process, and improve decision making and fairness of credit union-to-bank merger proposals.

Below, we offer our comments on specific aspects of the proposed regulatory changes.

Responsibility of Board of Directors

NCMT supports the proposed §701.4(a), which clarifies that the responsibility of credit union directors is non-delegable. In some cases that NCMT has observed, directors appear to have abdicated their responsibility to act in the best interests of the members, and appear not to have undertaken comprehensive study to determine that a certain merger or conversion is the most beneficial course of action for the member-owners.

We strongly support NCUA's clear affirmation in §701.4(b)(1) that directors and management act "in the best interests of the membership." In our observation, most arguments that conversion advocates have made to credit union members portray a conversion or merger as beneficial to the institution (e.g., it may allow the institution grow to a certain size, or compete in certain markets), without explaining how a conversion benefits

the members—the owners of the credit union. As NCUA observes, “A lack of focus on the interest of the membership makes it easier for officials and management to make decisions that benefit themselves personally, even if those decisions are not necessarily in the best interest of the membership as a whole” (page 5). NCMT believes that NCUA’s proposed language will clarify that directors have a legal responsibility to work for the best interests of the membership.

Likewise, NCMT believes the proposed §701.33(c)(5) is both valuable and prudent. The proposal will prevent Federal credit unions from indemnifying officials or employees from personal liability for decisions that affect the fundamental rights of the credit unions members, if the those decisions constitute gross negligence, recklessness, or willful misconduct. NCMT disagrees with the position that decision makers should be protected from the consequences of acting with gross negligence, recklessness, or willful misconduct. Rather, we support NCUA’s proposal that credit union members should be protected from gross negligence, recklessness, or willful misconduct of their elected or appointed leadership. Furthermore, we believe that the legal criteria of gross negligence, recklessness, or willful misconduct is a sufficiently high bar that it will not inconvenience employees or directors, or impede their decision making.

NCMT also finds good reason to support the proposed §701.4(d), which clarifies that, when a credit union director relies on advisors such as staff and outside consultants, he or she must review the advisor’s recommendations and consider the qualifications, conflicts of interest, or vested interest the advisor has. NCMT has observed credit union directors ignoring expert and disinterested advice, and instead relying on the advice of parties that stand to benefit financially from a conversion. This includes executives who could benefit personally from conversion in the form of stock gains, bonus, and compensation packages, as well as consultants, investment bankers, and attorneys who make their living assisting with credit union conversions and mergers. NCMT agrees with NCUA’s position that directors should, of course, be free to consider the advice of executive staff or paid outside experts. But the interests of these advisors also must be considered.

#### Electoral Process for Conversions and Mergers

NCMT's experience with past credit union to bank conversions has raised particular concerns about the viability of the existing election process, and we welcome NCUA's proposals to address the conversion election process. First and foremost, we strongly support the changes to §708a.101 that eliminate credit union management's access to periodic voting tallies. Access to these tallies has severely compromised the fairness of past elections. Access to a periodic tally of the vote requires pro-conversion management to restrain itself from attempting to manipulate the results of the election. We have observed cases where, apparently because voting tallies indicated that the member-owners opposed converting, management has accelerated spending of the credit union's net worth on advertising and targeted voter mobilization to increase the likelihood of a pro-conversion result. This biases the election process and wastes the credit union's member-owned resources.

NCMT does not support NCUA's proposal in §708a.101 that management continue to have access to the names of members who have not yet voted. Simply put, it is inherently unfair for pro-conversion management to have running access to voter information unavailable to members who oppose the conversion. As NCUA notes in the discussion of §708a.101, "some credit unions use this interim vote information for soliciting only voters likely to vote in favor of the conversion" (page 15). Unfortunately, NCMT believes this unfair practice will continue under the proposed rules. Furthermore, even if opposition members were granted equal access to updated voter roles, they could not effectively use that information. This is because credit union members do not have management's ability to use credit union's staff and financial resources to telephone members, send targeting mailings or emails, speak with members at credit union branches, or buy advertisements or telemarketing services.

NCMT recognizes the importance of member participation in elections, and believes that the duty of credit union management is to ensure that the views of all member-owners are represented. If management believes it is necessary to contact members and encourage them to vote, in addition to the encouragement provided by the 30, 60, and 90 days mailings, management should contact all members equally, or at least all members who have not yet voted. We would support allowing management to provide an election reminder notice to the independent entity managing ballots, and asking the independent entity to mail the notice to all members who have not yet voted. This would maintain the integrity of the election.

Also, it is unclear under the proposed §708a.101 whether credit union management is required to inform the member-owners of the results of conversion or merger elections. In discussion of these proposed rules, NCUA objects to a case where "management refused to disclose the results of the vote, in terms of the votes for and against the conversion, to its member-owners..." (pages 15-16). Indeed, refusal to release tallied election results has become common for elections where members voted against management's proposal. Election results were not released following the elections at Lafayette FCU, First Basin CU, and KV FCU. While the proposed definition of "conducted by an independent entity" in §708a.101 states that "the independent entity will certify the final vote tally in writing to the credit union and provide a copy to the NCUA Regional Director," it does not appear to require management to disclose the results of the vote. NCMT recommends that credit unions be required to inform the members of the election results by mail, though we would also support a less expensive means of communication in order to preserve credit union resources.

The cancellation of elections without disclosing the vote as also been problematic, such as the case NCUA identifies where "management stopped the vote because the running vote tallies management was receiving from the election tellers were nearly two-to-one in opposition to the conversion" (page 15). In the proposed regulations, this worrisome occurrence is not addressed. It is not satisfactory for credit union management to cancel an election and refuse to tell the member-owners the results, and it may provide management opportunity to escape accountability by casting blame for the cancellation of the election on the members themselves. NCMT suggests that NCUA require that if an election is cancelled, the results of the vote at the time of cancellation must be reported to NCUA and announced

to the membership by mail. Management would likely mail members notice of such a cancellation in any event, and so including the vote tally should not be a burden.

### Disclosures

NCMT supports the requirement in §708a.104(5) that management disclose the estimated cost of conversion, and strongly recommends that the NCUA require that this estimate be updated for inclusion in the 30, 60, and 90 day mailings. In most of the conversion proposals where member-owners organized an active campaign to preserve their credit union's co-op structure, management has responded by organizing similarly active pro-conversion campaigns, including additional mailings and advertisements. The costs of these campaigns may be substantial, unanticipated, and not included in earlier estimates. Particularly because these expenses are being paid using member-owned resources, and may be a factor in member decision making about the proposal, membership should be kept informed. Requiring updated and accurate information would not be an undue burden, as management should be tracking the expense of such a campaign and can include the information in the mailings already required by NCUA.

We believe the wording to the proposed credit union-to-bank merger disclosure §708a.305(d)(2) is inaccurate. As proposed, it requires a "clear and conspicuous disclosure that the merger could lead to members losing all of their ownership interests in the credit union if the bank subsequently converts to a stock institution and the members do not purchase stock." However, the loss of ownership is not contingent on the decision not to purchase stock. Put plainly, if one needs to re-purchase something they do no longer own it. At the moment a mutual bank converts to a stock bank, the former credit union members' equity is effectively erased. Members cannot avoid losing their ownership; they only have opportunity to buy ownership in the new institution. We recommend disclosure §708a.305(d)(2) read, "...the merger will cause members to effectively lose all of their existing ownership interests in the credit union if the bank subsequently converts to a stock institution. Members will have the opportunity to buy stock ownership." Any other language in §708 implying that mutual holders do not effectively lose their ownership stake in a stock conversion should be similarly amended.

### Credit Union to Bank Mergers

NCMT strongly supports NCUA's proposed regulations of credit union-to-bank mergers, as described in §708a Subpart C. The merger proposals we have observed thus far have been troubling because they have appeared to benefit the bank significantly, but do not appear to similarly benefit the member-owners of the credit union. In these proposals, members lose the benefits of competition and choice of two different financial institutions. For example, after a merger members can no longer obtain a car loan from the credit union, if that is the most advantageous option, and a home loan from the bank if the bank's interest rate on that product is lower. This loss of the credit union as an option can effectively equate to members being charged higher rates on loans and receive lower returns for deposits, without receiving any significant benefit in return. Becoming a mutual holder of the bank can not be considered

a compensating benefit--credit union members could already join the bank if they desired. NMCT believes these regulations provide needed structure for the merger process to preserve credit union member benefit.

In particular, we support the process of compensating credit union members for their equity, as modeled by Nationwide Federal Credit Union's merger. We believe credit union members are well served by the requirement in §708a.304(g)(1), by which "the Region Director must disapprove the proposed merger if: (i) The merger payment offered by the bank to the members is less than the merger valuation, absent some additional, quantifiable benefit to the members from the selected merger partner." We likewise support the disclosures described in §708a.304(d), §708a.305(c)(4) and §708a.305(d)(6). NCMT believe these regulations will deter merger proposals which benefit the bank's owners without appropriately benefiting credit union members.

When NCUA assesses "additional, quantifiable benefit to the members from the selected merger partner," under §708a.304(g)(1), we believe it is important that only benefits newly available to the membership be considered. For example, if the bank offers higher interest rates on some deposit products than the credit union does, this could not be considered a benefit to members if they could already join the bank to obtain these rates without a merger ever taking place. NCMT strongly suggests that NCUA only permit newly available benefits to be weighed against the valuation of member's ownership stake.

NCMT strongly supports NCUA's proposal in §708a.303 that credit unions proposing to merge into a bank obtain a merger valuation, as defined in §708a.301 as "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." To make an informed decision about charter change in the best interests of the membership, such a valuation is vital.

#### Merger Voting Participation Threshold

NCMT does not believe the 20% vote participation threshold in §708a.306 is sufficient for a change as drastic as a credit union changing its charter, regulator, the rights afforded to ownership, its governance structure and personnel, and merging into another existing financial institution.

Charter changes governed by other regulatory bodies generally require the approval of a majority of all potential voters, if not more. For example, when a state or federal mutual savings bank converts to stock form of ownership under the Office of Thrift Supervision, such a change must be approved by 50% + 1 of all outstanding votes. When a state bank converts to a national bank under the OCC, 51% of all voting stock must approve of the change. When the process runs the other direction and a national bank converts to a state bank, 66.67% of all outstanding stock must approve. However, under the proposed rules, a credit union could merge into a bank with the approval of only 10% + 1 of its members (assuming the other 10% vote in opposition). This does not sufficiently protect credit union member interests.

NCMT is aware that NCUA's recommendation sets a higher threshold than required for credit unions converting to a mutual savings bank charter under 12 U.S.C. 1785(b)(2)(B). Since the passage of HB 1151 in 1998, credit unions have been permitted to convert to banks with the approval of only a majority of voting members, possibly as few as five out of eight people. This also is too low a bar for a change of this magnitude, particularly for a charter change that has the potential for insider enrichment and member-owner loss.

NCMT urges congress to revise 1998's HB 1151, the Credit Union Membership Access Act, and allow NCUA to institute a reasonable voter participation requirement for credit union to bank conversions. We believe a reasonable threshold would require a majority of all members eligible to vote to approve a conversion. This was the requirement before HB 1151.

In conclusion, we would like to reiterate our support for NCUA's proposed regulations. Thank you for this opportunity to comment.

Sincerely,

/s/

Randy Chambers  
National Center for Member Trust