Delivered via e-mail to: regcomments@ncua.gov

August 7, 2017

Subject:

Marvin C. Umholtz Comments on Voluntary Mergers of Federally Insured Credit Unions

Addressed to:

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

I thank the National Credit Union Administration (NCUA) Board for the opportunity to provide comments about the Notice of Proposed Rulemaking concerning the proposal to revise the procedures a federal credit union (FCU) must follow to merge voluntarily with another credit union.

According to the NCUA Board's summary, the proposal under consideration will "…(1) revise and clarify the contents and format of the member notice; (2) require merging FCUs to disclose all merger-related financial arrangements for covered persons; (3) increase the minimum member notice period; and (4) provide procedures to allow reasonable member-to-member communications regarding the proposed merger. The proposed changes also make conforming amendments to NCUA regulations governing termination of federal share insurance when the continuing credit union is not an FCU."

Unfortunately, the results from actually implementing this "anti-voluntary merger" proposal would be extremely unreasonable, and would be in direct disregard of applicable statutory guidance.

The views expressed in this comment letter to the NCUA Board represent my own professional opinion and do not necessarily reflect the opinions of any client with which I might be affiliated. I serve as President & CEO of Umholtz Strategic Planning & Consulting Services located in Olympia, Washington. Current and former clients include credit union industry and banking industry organizations in the United States.

Assisting credit unions to voluntarily merge is not part of my consulting services book of business; however, merger as a strategic growth option is often discussed with clients in the context of exploring business tactics and objectives. As a matter of public policy, the NCUA Board should be making it significantly easier for credit unions to merge rather than making it dramatically harder to merge.

Summary of Umholtz's Key Points about the NCUA Board's Proposed Voluntary Merger Rule

- The proposed voluntary merger rule is among the worst NCUA-proposed rules that this forty-years-plus veteran of the credit union industry has ever seen.

- The NCUA Board should be aggressively reversing the former Obama administration's regulatory assault on credit unions and the consumers that they serve, not adding to the counterproductive compliance burdens represented by this [anti-]voluntary merger rule proposal.

- Without the right-scaling that unfettered voluntary mergers can bring, the smaller credit unions in the U.S. will be unable to proactively navigate the inevitable catastrophic compliance collapse.

- What are the real reasons that the NCUA Board, the NCUA senior legal staff, and the cheerleaders for the anti-voluntary merger rule within the credit union industry want to freeze-out credit union boards from self-selecting their own merger partners?

- Very few within the credit union industry have figured out the full ramifications of this proposed rule. And those that have made an attempt at doing so have focused on the "compensation straw man" rather than the more substantive "poison pill" that is the member-to-member communication aspect of the proposal.

- In what other business does the customer become the veto concerning structural and change-in-control decisions? Does the NCUA Board sincerely consider this proposed process to be safe and sound governance?

- Before 2017 is over, and in the worst case scenario, the NCUA Board will have made all voluntary mergers as difficult to pull off as a conversion from a credit union charter to a mutual savings bank charter. And there have not been any successful conversions for many, many years.

- The NCUA's proposed voluntary merger rule seeks fully informed members, yet it is unlikely to produce high-quality information for even a small fraction of those members to ponder notwithstanding mandates or incentives.

- The NCUA's blatantly elitist bias against mail ballots astonished me on so many levels. Since that point of view matches the point of view of persons who constitute the most zealous within the credit union industry, the logical conclusion is that the NCUA suffers from "regulatory capture."

- Once the federal government takes on the role of deciding what's best for any of this nation's citizens, American's personal liberties and individual consumer choices are coercively shoved down the proverbial slippery slope.

- The murkiness of the metrics become exponentially complex when "members' best interests" and "fully-informed" are comingled – providing a fertile minefield for the judiciary to explore for "arbitrary and capricious" illogic. [And may the *Chevron* deference be forever condemned for the violation of the U.S. Constitution that it most assuredly is.]

- The proposed anti-voluntary merger rule is, for all practical purposes, a sure-fire method for the NCUA to secure its monopoly on allocating merger winners and losers.

- The idea that credit unions, or even that SEC-regulated firms, should be controlled by individual shareholders (credit union depositors of as little as $5) is increasingly viewed as peculiar, or even dangerous.

- The Office of the Comptroller of the Currency seems to believe that individual depositors do not have any claim on a mutual savings bank's net worth unless it is being totally liquidated, nor do members' opinions appear to have much of an influence regarding a merger.

- The NCUA Board's continued insistence on the for-profit ownership interpretation applying to shared cooperative "ownership" [if even that legally exists] places the credit union charter at increased risk for governance instability and severely restricts each credit union's strategic options.

- The proposed voluntary merger rule appears erroneously premised upon the belief that a single credit union member's opinion on a merger 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.

- 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.

- Not only should the NCUA Board not adopt the clearly ill-advised [anti-]voluntary merger proposal, the NCUA Board should also take a cold, hard look at its hopelessly-anachronistic governance rules.

Policy Position Statement Concerning the NCUA Board's Voluntary Merger Proposal
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 this convoluted and inevitably costly rule.

The voluntary merger changes currently 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 voluntary merger rule makes 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. More NCUA time and resources should be spent monitoring the credit union industry's safety and soundness and mitigating the potential credit union losses rather than dictating misguided notions of ideological correctness as exhibited by this and other NCUA rules.

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 requirements 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 credit unions serve.

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 union's boards of directors.

The Unintended and Intended Consequences Will Inevitably Be Counterproductive
Although on its surface the NCUA Board's voluntary merger proposal sounded benign, it was far from innocuous – it was among the worst NCUA Board proposed rules that this forty-years-plus veteran of the credit union industry has ever seen. Not only was the proposed rule filled with potentially "unintended consequences," but since the proposed rule's public emergence, I have suspected that those unpleasant consequences were deliberately intended to place an extreme chill – if not an outright deep-freeze – on voluntary mergers that included federally chartered credit unions.

This meddlesome rulemaking on voluntary mergers will have the same functional effect as would unrealistic "price controls" on credit union products and services – destructive and debilitating. In other words, the proposed rule is a throwback to the bad old days of interventionist regulatory overreach that was symptomatic of the Obama administration rather than the right-sizing of regulatory expectations heralded by the Trump administration. The Trump administration appears to be razor-sharp serious about alleviating unnecessary regulatory burdens placed on the American people. This proposed voluntary merger rule will double-down on those stifling burdens characteristic of the repressive past.

The NCUA Board should be aggressively reversing the former Obama administration's regulatory assault on credit unions and the consumers that they serve, not adding to the counterproductive compliance burdens represented by this [anti-]voluntary merger rule proposal. Frankly, the NCUA's merger rule is very cumbersome in its existing form and could use a thorough streamlining, notwithstanding the proposal. For all federal executive branch agencies – whether so-called “independent” or not – an “*in loco parentis*” [Latin for a humiliatingly-embarrassing ‘in lieu of parents’] “I’ve got a pen and I’ve got a phone” attitude doesn’t cut it anymore.

Application of the Rule to Smaller Credit Unions and State Charters Would Be “Catastrophic”
Without the right-scaling that unfettered voluntary mergers can bring, the smaller credit unions in the U.S. will be unable to proactively navigate the inevitable catastrophic compliance collapse.

It would appear that even in their most desperate hour, those determined visionaries who would lead these smaller institutions forward are unfortunately surrounded by a self-anointed group of retrograde, self-protecting vested interests, and their political handmaidens, who are eager to impose their own hard-left narrative upon the duly elected officials who run these merger-seeking credit unions. That deliberately-divisive, anti-voluntary merger narrative must not be allowed to prevail.

And when it comes to so-called “member protection” issues so dear to the anti-merger crowd, it would appear that credit union members need to be protected from an apparently gullible and clearly overly-aggressive NCUA.

That “protection” from the NCUA is especially needed by those members served by federally insured state chartered credit unions that the NCUA Board was apparently considering including in the future revisions to this Notice of Proposed Rulemaking. The NCUA has already intruded beyond all respectful levels into state credit union matters. Applying this counterproductive anti-voluntary merger proposal on state chartered federally insured credit unions would add to the ever-growing pile of dual chartering system insults.

Meaningless Hyper-Disclosures Identify Targets for the Credit Union Hard-Left to Bully
The passage of the partisan-on-steroids, still-controversial, and probably-unconstitutional *Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010* included inappropriate [and ultimately ineffective yet costly] Democratic Congress-championed edicts like the Congo conflict minerals disclosure provision and the CEO vs. rank-and-file employee compensation ratio disclosures, among other politicized insertions that had nothing to do with fixing the 2007-2008 financial crisis. The Democratic Party’s U.S. House and U.S. Senate majorities in 2010 taught the financial services industry that the primary purpose of meaningless hyper-disclosure was to identify targets for the hard-left to bully.

While the NCUA Board and the NCUA’s legal department staff are adding mandatory disclosures to “fully-inform” credit union members, perhaps they should add these *Dodd-Frank Act* mandates as well. What’s next? *Community Reinvestment Act*-like performance measures? Credit union staff diversity quota disclosures? Small business lending to women and minorities metrics? The ‘politically correct” mandates list goes on and on. What does it take to satisfy the NCUA’s politically correct fully-informed expectations?

Perhaps all of the voluntary merging and continuing credit unions’ individual board of directors’ partisan political affiliations should be disclosed to members as well. Those disclosures of affiliations would be material to me and possibly many other credit union members regarding any merger vote in which they might participate as a member. I’m not certain that I would trust the decisions made by any hard-left blue-staters. Without these and other personally-important details, I couldn’t make a “fully-informed decision” as to the efficacy of the merger should the political leanings of the leadership be insufficiently hard-right in tenor. With a rabidly-divided population likely also members of credit unions, partisan affiliations could be vitally important information affecting how a member would vote in a fully-informed manner.

Add Hard-Right Disclosures to Ensure “Fair and Balanced” Fully-Informed Membership
As a member of four credit unions, this correspondent could have the opportunity to instigate plenty of improper mischief under the NCUA Board’s customer-empowered merger veto rule proposal. Or if the NCUA Board is serious about transparency, perhaps any member of the general public should be empowered to raise concerns and/or protest a credit union-to-credit union merger on any partisan ideological grounds. Perhaps the NCUA Board should require that the merger plan be disclose in a newspaper of public record, or posted on a public website like NCUA.gov.

And while new disclosures are being contemplated, proper honesty would require that the NCUA regional director officiating the voluntary merger process disclose his or her political affiliation and partisan biases to the membership in order to ensure a fully informed membership. The regional director's partisan skew would provide the merging credit union's and the dissident members' attorneys with equal access to useful fodder for lawsuits.

It would also be more honest for the NCUA Board to remove all currently-mandated disclosures, and replace them with one informing the members that as an alternative to the merger, the members could propose to liquidate the institution and receive a share of the credit union's net worth based upon individual deposits. Such a disclosure would likely cause disruption of sorts, but disruption no worse than that which would likely result from this proposed rule.

Regardless of the amount and the number of disclosures, compelling questions remain that have not been addressed by the NCUA Board: In what other business does the customer become the veto concerning structural and change-in-control decisions? Does the NCUA Board sincerely consider this existing voluntary merger rule and proposed voting process to be safe and sound governance? The NCUA Board members should not believe such is so.

In all seriousness, I hope that the NCUA Board understands the "slippery slope" on which its existing voluntary merger rule currently stands – and which it proposes to muddy-up to the extreme with this new proposal.

What is the Real Motivation for the Anti-Voluntary Merger Rule?

Although I am by nature reluctant to ascribe motives to others, nonetheless speculation abounds among colleagues, industry analysts, and credit union CEOs critical of the NCUA's proposed voluntary merger rule.

Some individuals within the credit union industry might desire to make voluntary mergers more difficult in order to generate more demand for specialized consultants and merger attorneys [both pro-merger and anti-merger]. That is the classic definition of self-interest, but an allowable homage to free enterprise nonetheless.

Other individuals might be very curious about what other credit union staffers receive in compensation. The more the number of staff members whose compensation must be disclosed related to a merger, the more invasive data the compensation-curious individuals can drool over and tut-tut over. Perhaps their curiosity could be sated if the NCUA would post all voluntary merger deals on the NCUA.gov website as a service to the public.

There might be still others who are concerned about the damage that will be done by the sustainability-threatening, exponentially-growing regulatory and risk-management compliance expectations for small credit unions by federal regulators, as well as by the state supervisors – especially as it pertains to state chartered credit unions. Huge numbers of these smaller credit unions are not currently in compliance and do not have the revenues to invest to become compliant. Merger or liquidation are their only options. Shouldn't the leaders at these credit unions be given what little choice that they have left to them to steer their institutions toward a better solution rather than to have a NCUA "death panel" mandate the nature of and the timing of their conclusion?

When one finds the NCUA's publicly-provided rationale difficult to digest, it is not unusual to look across the table for alternative motives upon which to chew. What are the real reasons that the NCUA Board, the NCUA senior legal staff, and the cheerleaders for the anti-voluntary merger rule within the credit union industry want to freeze-out credit union boards from self-selecting their own merger partners?

This proposed voluntary merger rule is the wrong thing to do at the very wrong time to do it. So the NCUA Board should not do it.

Member-to-Member is the Poison Pill of NCUA's Proposed Rule
Very few within the credit union industry have figured out the full ramifications of this proposed rule. And those that have made an attempt at doing so have focused on the "compensation straw man" rather than the more substantive "poison pill" that is the member-to-member communication aspect of the proposal.

I doubt that any credit union member joined the credit union – providing his or her residential address and email address – so that he or she could receive unsolicited opinions from other members concerning mergers or other topics affecting the organizational structure of the institution. Upon receiving such an unwanted opinion, most members would likely be irritated, offended, annoyed, or even appalled by the misapplication of the financial services relationship that he or she had entrusted to the credit union. The potential reputation risk to the credit union could be very harmful.

Once in place as proposed, or as expanded to include federally insured state chartered credit unions as well, the NCUA regional directors will become like banana republic dictators controlling their fiefdoms by rewarding their loyal cronies with the spoils of involuntary mergers [because there will be no competition from voluntary mergers].

The rulemaking process is in the early stages, however, it is likely to be finalized by the end of 2017. That means before 2017 is over, and in the worst case scenario, the NCUA Board will have made all voluntary mergers as difficult to pull off as a conversion from a credit union charter to a mutual savings bank charter. And there have not been any successful conversions for many, many years.

Unfair Finger-Pointing at Pennsylvania CUs Fueled NCUA Voluntary Merger Curbs
During the brief open meeting on May 25th, the NCUA's legal staff presentation emphasized the merger-related compensation part of the proposed rule. The merger-related compensation of merging credit union officials had also been sensationalized in near-hysterical, rabble-rousing opinion essays in the run-up to the NCUA Board meeting. However, unlike many of the recently-proposed NCUA Board rulemakings that have received hundreds, even thousands, of comment letters, it appears that this proposed rule only garnered dozens. It would appear that this grave risk to the credit union system is not top-of-mind.

The *CUToday.info* had run a series of articles highlighting the conflicts surrounding an otherwise routine voluntary merger procedure engaged in between Carlisle, Pennsylvania-based, $109 million in assets, 11,025-member Cornerstone Federal Credit Union www.cornerstonefcu.coop and Harrisburg, Pennsylvania-based, $471 million in assets, 53,426-member Belco Community Credit Union www.belco.org. Both credit unions' origins were rooted in serving telephone company employee groups. The NCUA had neither confirmed nor denied that the Cornerstone FCU – Belco Community CU controversies had anything to do with the promulgation of the new voluntary merger proposed rule, but for even the casual observer it was a difficult connection to ignore.

According to one article, a group of anti-merger dissidents led by the Cornerstone FCU's retired former-CEO, Dave Keffer, had even gone so far as to drag the rogue federal agency – the Consumer Financial Protection Bureau (CFPB) www.consumerfinance.gov, as well as U.S. Senator Elizabeth Warren (D-MA), the hard-left strident defender of the highly-partisan, still-controversial, and probably-unconstitutional *Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010*, into the credit union's internal squabble http://www.cutoday.info/THE-feature/NCUA-Says-No-To-Group-s-Request. Involving the CFPB and Senator Warren was a stupid move to say the least; it revealed either a political naiveté or a deliberately hard-left partisan slant to the dissidents' merger disruption tactics. By that ill-advised action, the Cornerstone FCU merger, as well as the NCUA Board's proposed voluntary merger rule, have now become toxically partisan.

Overarching Draconian Rule Not Appropriate When Surgical Remedies Available
One can also wonder how the previously responsible members of the Cornerstone FCU board of directors, who employed and supported the former CEO for so many years, suddenly morphed into "evil-doers" during the subsequent two years since the now-dissident former CEO's retirement, such that the board members proposed a merger that was somehow not in the "best interests of the members" as the anti-merger

dissidents claimed. Somewhere in this good-turned-evil credit union board equation there existed a high degree of cognitive dissonance. In this case, there appeared to be insinuations of corruption for which there existed zero evidence. Why or how that particular situation required a draconian move to freeze-out voluntary mergers baffled me. Weren't more surgical remedies available to the NCUA and others involved?

If there exist only a few repeating offenders, why won't the NCUA Board Members and the senior NCUA staff "transparently" say the credit unions' names publicly? Rather than write an overreaching rule governing all voluntary mergers, perhaps the NCUA Board should have simply called the cops and jailed the evil-doers from whichever side of this Pennsylvania spat the "evil" happened to be occurring. In the absence of formal charges, perhaps the evil-doers could instead be shackled and pilloried in the Carlisle, Pennsylvania town square – or better yet, shackled and pilloried at the King Street Metro Station in Alexandria, Virginia in direct line-of-sight of the NCUA's headquarters.

Since the May 25th NCUA Board meeting and the adoption of the proposed voluntary merger rule, the dissident group at Cornerstone FCU had appealed to the NCUA Board to reconsider the Pennsylvania merger http://www.cutoday.info/THE-feature/Committee-Hoping-For-Agency-Response – which passed by a membership vote of 1,100 to 630 in early March 2017. Reportedly only 1,730 (15.7%) of the Cornerstone FCU's 11,025 "owners" bothered to vote either by mail or in-person.

Doubtful Additional Cubic Feet of Disclosures Would Lead to Different Vote Outcome
Although some observers might interpret the low participation level as an "I don't care ballot," it could also be interpreted as "I was too busy to vote;" or as a vote interpreted to mean "If it passes, fine, and if not, that's OK, too." I doubted that the non-voting Cornerstone FCU members lacked sufficient information concerning the merger to make an informed decision [as the dissidents' and the NCUA's false meme contended]. After reading about the voting results, I also doubted that requiring additional cubic feet of disclosures concerning employee compensation would have made a material difference in the vote tally, or in the vote participation level.

Perhaps the NCUA Board should require that credit unions engaging in voluntary merger votes incentivize all credit union members to participate with a cash prize. After all, during the recent United Kingdom election, the Labour [British spelling] Party's promise of free college tuition certainly brought out the younger voters [who voted heavily for Labour's candidates]. And prize-linked savings contests are already the rage at credit unions, so the transition to this proposed prize-based NCUA mandate for voluntary merger voting would be an easy one.

The NCUA's proposed voluntary merger rule seeks fully informed members, yet it is unlikely to produce high-quality information for even a small fraction of those members to ponder notwithstanding mandates or incentives.

CU Members' Best Interests, Fully-Informed & Other NCUA Merger Rule Fallacies
I also found it disturbing that the NCUA Board's explanation of the proposed voluntary merger rule's intent stated, "The Board has observed in a recent merger a significant disparity between the high number of members voting to approve the merger by mailed ballot compared to the low number of members voting to approve the merger in person at a member meeting. While such procedures are permissible under NCUA's regulations, the Board is concerned that members voting by mailed ballot do not benefit from the rigorous debate that may take place during a member meeting where members are free to discuss the proposed merger openly with management or the directors of the FCU."

The NCUA's blatantly elitist bias against mail ballots astonished me on so many levels. Since that point of view matches the point of view of persons who constitute the most zealous within the credit union industry, the logical conclusion is that the NCUA suffers from "regulatory capture."

In the State of Washington, all of the elections for public officials are done by mail ballot – there are no polling stations on Election Day. To suggest that any Washington citizen's mail ballot candidate selections, as well as decisions concerning special referendums or other ballot issues, were not rigorously considered, is an insult of the highest order.

Additionally, the NCUA Board's inference that somehow an in-person meeting would result in a situation where credit union members would "benefit" from a "rigorous debate" suggested that the NCUA Board members [and probably the NCUA senior staff] have never experienced a "real world" meeting where people mostly **pool** their shared ignorance with their fellow members. Sadly, such meetings are too common. The NCUA's comment would be laughable if it wasn't so destructive.

Even if the NCUA would effectively police the outrageous comments made by dissidents prior to the meeting, which I wholeheartedly doubt they would even if they could, the verbal comments made by dissidents on-site at a special meeting to discuss a voluntary merger would be impossible to prudently manage by anyone. It would not be a "rigorous debate," it would be a donnybrook.

Each Member's Best Interests Are His or Her Own to Define

The counterproductive "best interests of the members" phraseology currently used by the NCUA is secret code for "whatever the NCUA legal department staff and the relevant NCUA regional director say it is."

Seriously now, what does that phrase mean and how do you measure it? Are the best interests of each of the 11,025 members of Cornerstone FCU exactly the same regardless of whether they are a borrower or a saver? A man, a woman, or whatever? An adult or a child? A hard-left Democrat or a hard-right Republican? Have a high-income or a low-income? Should the federal government make this "best interests" decision or should each individual make this decision for themselves?

Although used in the context of channel access to products and services rather than a membership vote, the Navy Federal Credit Union's CEO J. Cutler Dawson was quoted in a recent *CUToday.info* article http://www.cutoday.info/THE-feature/CEO-Talks-Key-Decisions-That-Have-Driven-Growth as stating, "Our members are motivated by different things." That insightful statement carries added weight since the Virginia-headquartered, $81.5 billion in assets Navy FCU had nearly 7 million members. It would be extremely doubtful that each of those 7 million member's "best interests" were the same. And while discussing the Navy Federal Credit Union, imagine if the credit union needed to seek a venue to seat its seven million members under one roof to hold an in-person membership discussion to confirm a merger plan – unfathomable.

Credit Union Boards of Directors Know Members Better Than NCUA

The "members' best interests" is a very murky idea that does not belong in the federal credit union statutes or in the NCUA rules. Determining the members' best interests is a terrible burden to place on a specific credit union's board of directors; however, I cannot think of any group better situated then that board to make such a decision – and that decision should be made without the threat of the NCUA Board, the NCUA legal department, or the NCUA regional directors second-guessing them. Once the federal government takes on the role of deciding what's best for any of this nation's citizens, American's personal liberties and individual consumer choices are coercively shoved down the proverbial slippery slope.

In the NCUA's proposed voluntary merger rule, the rule's background statement had the audacity to suggest, "Some credit unions may find themselves in the position of being a potential merger partner with more than one credit union. In this position, management must appropriately evaluate competing opportunities and consider which merger partner would be in the members' best interests in terms of member philosophy and continued or expanded products or services." A footnote cited a 2006 rulemaking and 2011 guidance.

Not only is "members best interests" a murky idea, but setting it in terms of "member philosophy" further obfuscated the concept. How nebulous can that member philosophy concept get? Is that defined in the statutes somewhere? Does the NCUA accept the trade associations' various interpretations of the term, and if so, is that "philosophy" as defined in 1934, 1954, 1974, 1994, 2014, or when? Such a determination is like nailing Jell-O to the wall.

Products & Services Snapshots Are Deceptive When Used in "Best Interest" Comparisons
Since the NCUA's existing and proposed voluntary merger rule's use of the terms are related to products or services that cannot be guaranteed past the short term future, even talking about "members best interests" publicly seems disingenuous. Requiring that illustrations of "members' best interests" be disclosed in the merger agreement, as well as in disclosures or other communications, seems inappropriate and misleading.

Such products and services comparisons when disclosed to credit union members are inherently snapshots in time and mere statements of intent rather than contractual promises. Providing absolute guarantees about keeping branches open forever, or for perpetually offering specific products or services, would be the height of irresponsibility. Even including such items in mandatory disclosures appears deceptive. My concepts of members' best interests and the NCUA Board's concepts of credit union members' best interests are unlikely to ever coincide. So why even talk about them?

The murkiness of the metrics become exponentially complex when "members' best interests" and "fully-informed" are comingled – providing a fertile minefield for the judiciary to explore for "arbitrary and capricious" illogic. [And may the *Chevron* deference be forever condemned for the violation of the U.S. Constitution that it most assuredly is.]

NCUA Will Never Get Fully-Informed Right; nor Should the Agency Be Allowed to Do So
What it takes to be "fully-informed" is in reality in the eye of the individual beholder, and is not a universally-held legal concept cast in stone. The NCUA will never get it right as it pertains to each member at each credit union; and there is no clear and unassailable definition in the statutes or the rules. As historically implemented by the NCUA, applying the "fully-informed" test served to cement the agency's monopoly on selecting merger winners and losers.

This unrealistic fully-informed test was particularly useful to the dissidents who leveraged the member-to-member communication provisions found in the NCUA's existing credit union-to-mutual savings bank charter [anti-]conversion section of the NCUA's current rule that the NCUA Board proposed to transfer to the CU-to-CU voluntary merger rule. As implemented by the NCUA staff in charter conversion votes, a lone dissident member could promote lies, innuendos, and exaggerations to all other members with impunity, while the credit union's board of directors were forced by the NCUA to operate under what amounted to a severe gag rule of absolute silence.

This new proposal by the NCUA Board in no way qualified as deregulation, or as good public policy. The proposed anti-voluntary merger rule is for all practical purposes a sure-fire method for the NCUA to secure its monopoly on allocating merger winners and losers.

Who Really Owns Credit Unions?
In August 2011, the Filene Research Institute (FRI) www.filene.org released a no-nonsense study by former FRI executive director Bob Hoel entitled, "*Power and Governance: Who Really Owns Credit Unions*?" Among many other findings and observations Hoel wrote, "It is also popular for credit union CEOs, board members, trade associations, and regulators to proudly proclaim that credit union members own their credit union. Again, rhetoric fails to tell the complete story. Determining who controls capital is a key step in identifying the organization's authentic owner. Credit union CEOs and boards, like their corporate counterparts, play key roles in capital decision making."

Hoel also said, "In addition, government regulators exert extraordinary influence on capital levels and capital deployment. Members have almost no control over capital in most credit unions today. Regulators tend to act as though they own a credit union's capital…The extraordinary power of credit union regulators raises the distinct possibility that they are the true owners of the credit union. As noted previously, if the regulator or any other party controls the credit union's capital, it is, for all practical purposes, the credit union's owner."

Not Possible to View Members as the Credit Union's Owners
Hoel also wrote, "Given the power of boards, CEOs, and regulators over capital, it is not possible to view members as the credit union's owners in the classic sense. Member ownership rights are modest; some might even argue that they are trivial. Members cannot sell or otherwise transfer their theoretical share of ownership to others. They cannot withdraw their share of the credit union's capital when they move or when they terminate their membership. Their heirs do not have an equity claim upon their death. The only times that credit union members receive capital distributions are when the credit union is liquidated or when regulators conclude that the credit union is grossly overcapitalized and permit the credit union to make a special capital distribution. In most non-credit-union cooperatives, member owners have far greater power to transfer and redeem their ownership shares."

Hoel continued, "Four actors – CEOs, boards, regulators, and members – all have some power to control and deploy capital. One conclusion from this multipower arrangement is that the four are joint owners. An alternative view is that the true ownership is so vague and convoluted that no one owns the credit union. The credit union, in essence, owns itself, and it is a self-perpetuating entity."

OCC Said Mutual Savings Bank Depositors Do Not Own Institution's Net Worth
The misguided anti-voluntary merger champions who claimed that customers of not-for-profit, organized without capital stock, cooperatively-structured credit unions should have the same ownership rights (or even more rights in some cases) as do stockholders of publicly-held, Securities and Exchange Commission-regulated, for-profit companies, persisted in their calls for ill-advised increased federal government intervention (in this case, the NCUA's direct intervention) in the name of transparency and disclosure.

The idea that credit unions, or even that SEC-regulated firms, should be controlled by individual shareholders (credit union depositors of as little as $5) is increasingly viewed as peculiar, or even dangerous. Apparently in the credit union regulatory arena, quality controls on unbridled discourse have become an afterthought. Credit union mythologies appear to be more valued than truth-telling itself.

A recent article that appeared in the *Credit Union Journal* https://www.cujournal.com/news/lawsuit-over-mutual-bank-merger-comes-as-ncua-tackles-similar-issues?brief=00000158-73f9-d502-a5fd-7bfbd3d10000 that also was published in its sister publication, the *American Banker*, made the connection between the NCUA Board's proposed voluntary merger rule and a lawsuit filed in Missouri by two depositors in a merging mutual savings bank. The *Credit Union Journal* article stated, "First Federal Bank in Kansas City, Mo., is at the center of litigation that threatens to undermine what it means to be a mutual. Two former account holders of Inter-State Federal Savings and Loan Association of Kansas City, which merged into First Federal last year, filed a lawsuit in February in the U.S. District Court for **the** Western District of Missouri, claiming they were shortchanged by the merger." Will credit union depositors soon begin suing credit unions for similar reasons?

The *Credit Union Journal* continued, "The unusual case is drawing national attention, with the Office of the Comptroller of the Currency, the American Bankers Association and the Missouri Bankers Association filing briefs in support of First Federal. The suit is likely to be of particular interest to credit unions given that the National Credit Union Administration has recently proposed changes to how credit unions undergo voluntary mergers. Under the proposed rule, credit unions undergoing voluntary mergers would face a significant increase in the required disclosures of incentives provided board members and senior executives at merging CUs, along with establishing procedures to allow better communication between members in advance of merger votes. The concern in the Kansas City case is that a ruling in favor of Inter-State account holders could give more rights to mutual members which would, by extension, redefine what it means to be a mutual. For now, the rights for mutual members largely involve issues tied to electing directors, subscribing for shares and liquidation." That description of rights was much like the description of member rights at a mutually structured credit union. A mutual savings bank's net worth is built with net earnings and is collectively "owned" by its depositor-members – much like with credit unions.

OCC Rebuked Dissidents Seeking Distribution of Retained Earnings Following Merger
As explained by the American Bankers Association's (ABA) *Newsbytes* on May 18th, "In the case, *Chase v. First Federal Bank of Kansas City* http://bankingjournal.aba.com/2017/05/aba-occ-file-briefs-in-missouri-mutual-ma-litigation/#_ga=2.231037663.1958217739.1495201745-1380121422.1495201745, the plaintiffs [depositors Steven Chase and Shawn Penner] seek a windfall payout of the surplus of Inter-State Federal Savings & Loan Association of Kansas City, Mo., that was accumulated in the bank and invested in the community since 1889. The dispute arose when Inter-State merged with First Federal Bank of Kansas City in 2015. The plaintiffs, who were depositors in Inter-State, filed a lawsuit alleging that the merger was inequitable given the alleged $25 million in 'capital disparity' between the two institutions. First Federal argued that depositor plaintiffs have no enforceable 'ownership' interest in Inter-State or call on capital, and the case should accordingly be tossed…In a separate [friend-of-the-court] brief, the OCC argued that the plaintiffs' demand to a mandatory distribution of retained earnings contravenes OCC supervisory policy that, as a matter of safety and soundness, strongly favors retention of capital as a cushion against losses. Additionally, the OCC argued that members of mutual savings banks have no equity interest in the bank's retained earnings under federal case law and agency interpretation."

Office of Comptroller of the Currency Cited U.S. Supreme Court Ruling
The OCC's brief cited a U.S. Supreme Court decision addressing the nature of ownership in a mutual institution [*Society for Savings v. Bowers*, 349 U.S. 143,149-150 (1955)]:

> "The asserted interest of the depositors is in the surplus of the bank, which is primarily a reserve against losses and secondarily a repository of undivided earnings. So long as the bank remains solvent, depositors receive a return on this fund only as an element of the interest paid on their deposits. To maintain their intangible ownership interest, they must maintain their deposits. If a depositor withdraws from the bank, he receives only his deposits and interest. If he continues, his only chance of getting anything more would be in the unlikely event of a solvent liquidation, a possibility that hardly rises to the level of expectancy. It stretches the imagination very far to attribute any real value to such a remote contingency, and when coupled with the fact that it represents nothing which depositors can readily transfer, any theoretical value reduces almost to a vanishing point."

The OCC also cited several relevant cases from lower courts in several circuits:

> "The mutual form of organization is an odd duck. Nominally the customers own the mutual, but it is ownership in name only. They cannot sell what they 'own,' and if they withdrew savings they receive only the nominal value of the account rather than a portion of the mutual's net worth, which is valuable to them only to the extent it permits the bank to pay higher interest. *Ordower v. Office of Thrift Supervision,* 999 F. 2d 1183, 1185 (7th Cir.1993)
>
> "Although the depositors are the legal 'owners' of a mutual savings and loan association their interest is essentially that of creditors of the association and only secondarily as equity owners. Depositors' rights are circumscribed by statute and regulation. They are not allowed to realize or share in the profits of the association, but are entitled only to an established rate of interest. The depositors do not share in the risk of loss since their deposits are federally insured, and their only opportunity to realize a gain of any kind would be in the event the savings and loan dissolved or liquidated." *York v. Federal Home Loan Bank Board*, 624 F. 2d 495, 499-500 (4th Cir. 1980)

Credit Union Depositors Do Not Own the Institution's Net Worth
Apparently despite the U.S. Supreme Court's and other courts' perspectives, the NCUA legal staff thought that credit union members [holders of at least one "share"], as individuals, own the "mutual" credit union's net worth as if they were shareholders in a for-profit SEC-regulated company, and also think that members should, as individuals, be authorized to veto any voluntary merger. In contrast, the Office of the Comptroller of the Currency seems to believe that individual depositors do not have any claim on a mutual savings bank's net worth unless it is being totally liquidated, nor do members' opinions appear to have much of an

influence regarding a merger. The statutes provided the mutual institution's board of directors with the authorities and with the limitations by which they acted.

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

The existing 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" [if even that legally exists] 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).

Washington Appeals Court Ruling Confirmed CU Members Resemble Bank Depositors

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 the proposed NCUA voluntary merger rule – as well as to the NCUA's existing regulations concerning governance and conversions. The Court's points should be carefully considered before the NCUA Board finalizes the proposed rule.

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 not going to happen at a collectively-owned credit union in which an individual member typically receives a fair market value of zero for his or her intangible [possibly non-existent] share of ownership when leaving the credit union.

Credit Union Members Are Customers with a Few Voting Privileges

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 nearly 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 voluntary merger rule appears erroneously premised upon the belief that a single credit union member's opinion on a merger 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 Repeated for Mergers?
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 potentially the proposed new voluntary merger rule} 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 were 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. The OTS was subsequently merged into the OCC.

NCUA Promulgated Rules That Defied Congressional Intent
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 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 the obstructionist revised conversion 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 suggested that the NCUA would continue being nitpicky and excessively bureaucratic in its handling of notices, member communications, and voting in mergers and conversions. The new proposal affecting voluntary mergers requiring increased disclosures and member-to-member communications validated those fears.

Modernize, Repeal, and Rollback Existing NCUA Governance and Structural Change Rules
The NCUA Board should resist the temptation to overregulate in the manner described in the proposed rule. 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.

NCUA's Governance Rules Empowers Fringe Groups to Disrupt Credit Union Voluntary Mergers
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 seven 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 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.

Voluntary Merger Rule Will Make It Easy to Hijack the Credit Union
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 overregulation.

NCUA Board Should Not Adopt the Proposed Anti-Voluntary Merger Proposal
Not only should the NCUA Board not adopt the clearly ill-advised [anti-]voluntary merger proposal, the NCUA Board should also take a cold, hard look at its hopelessly-anachronistic governance rules. This overdue review should include its narrowly-drawn and borderline-ridiculous Federal Credit Union Bylaws, its statutorily-abusive anti-CU-to-bank conversion rules, and the many other rules [as well as scores of

antiquated statutes] that were promulgated in an era when credit unions were very unlike the very complex, widely-scrutinized, federally insured institutions that they have become today.

Adding additional burdens to governance, mergers, or conversions is the last thing the credit union industry needs at this time. With this proposal, 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 rule is based upon flawed concepts of member ownership of credit union equity and irresponsibly endows dissident members with the ability to derail structural changes that could benefit the institution and the vast majority of members.

Regardless of whether a credit union’s leaders have plans to merge with another credit union or simply want to preserve the strategic options for the future, they should be particularly disappointed in the NCUA Board’s regulatory overreaching. These proposed and the existing complex rules will not stop a credit union that is determined to merge, but the rules will certainly increase the cost of doing so.

Attorneys and/or merger consultants will have the most to gain since they will be able to justify significantly higher fees once the NCUA Board’s [anti-]voluntary merger proposed rule become final.

And, as one colleague remarked to me in reference to the voluntary merger proposal, “Maybe the NCUA Board has been soaking in the Hot Tub Time Machine.” It is past time that everyone in the credit union industry step out of that backwards-looking hot tub, dry off, and get properly dressed up for the realities of the 21st Century.

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

Sincerely,

Marvin C. Umholtz 08/07/17
analysis~advice~advocacy

Marvin C. Umholtz, President & CEO
Umholtz Strategic Planning & Consulting Services
1613 Easthill Ct NW
Olympia, WA 98502
(360) 972-5673 (cell #1)
(360) 972-5674 (cell #2)
marvin.umholtz@comcast.net
www.linkedin.com/pub/marvin-umholtz/10/909/bb9

Marvin Umholtz is president & CEO of Umholtz Strategic Planning & Consulting Services based in Olympia, Washington south of Seattle. He is an over 40-year financial services industry veteran who has held many leadership positions with credit union organizations, and with financial services industry vendors, during those years. A former association executive and lobbyist, he candidly shares his credit union industry knowledge and analysis with public policymakers, financial industry executives, and vendor companies. Umholtz also writes and distributes *CU Strategic Hot Topics*, a “clients and colleagues” newsletter that analyzes the actions of the National Credit Union Administration (NCUA), the Consumer Financial Protection Bureau (CFPB), the banking regulators, the Congress’ divisive partisan politics, the lagging economy, and the uncertainties in financial markets.