

of the Federal Credit Union Act (Act) concerning conversion of insured credit unions to mutual savings banks. 12 U.S.C. 1785(b). CUMAA required NCUA to promulgate final rules regarding charter conversions that were: (1) Consistent with CUMAA; (2) consistent with the charter conversion rules promulgated by other financial regulators; and (3) no more or less restrictive than rules applicable to charter conversions of other financial institutions. NCUA issued rules in compliance with this mandate. 63 FR 65532 (November 27, 1998); 64 FR 28733 (May 27, 1999).

It has been almost five years since NCUA first amended Part 708a to comply with CUMAA. In that time, NCUA has grown concerned that many credit union members do not fully appreciate the effect the conversion may have on their ownership interests in the credit union and voting power in the mutual savings bank.

Discussion

There are increasing indications that a high percentage of credit unions that convert to mutual savings banks have or will undertake a second conversion to become a stock institution. While it is certainly within the rights of the credit union membership to exercise their right to convert and change the structure of the institution, converting credit unions generally do not adequately discuss in the notice to credit union members the likelihood and ramifications of a second conversion to a stock institution.

While State laws may vary, under the Office of Thrift Supervision's regulations, there is no minimum waiting period for a newly chartered Federal mutual savings bank to convert to a stock institution. As a result, it is possible for a credit union that converts to a Federal mutual savings bank to attempt to convert to a stock institution in less than two years. In most cases, a conversion from a mutual savings bank to a stock institution will result in a loss of ownership interest for a majority of its members because most members do not purchase stock in the institution.

While CUMAA provides that an insured credit union may convert to a mutual savings bank without the prior approval of NCUA, it also requires NCUA to administer the member vote on conversion and review the methods and procedures by which the vote is taken. This is reflected in NCUA's conversion rule. The rule requires a converting credit union to provide its members with written notice of its intent to convert. 12 CFR 708a.4. It also specifies that the member notice must

adequately describe the purpose and subject matter of the vote on conversion. *Id.* In addition, a converting credit union must notify NCUA of its intent to convert. 12 CFR 708a.5. The credit union must provide for NCUA's review a copy of the member notice, ballot, and all other written materials the credit union has provided or intends to provide to its members in connection with the conversion. *Id.*

A converting credit union has the option of submitting these materials to NCUA before it begins to distribute them to its members. *Id.* This enables the credit union to obtain NCUA's preliminary determination on the methods and procedures of the member vote based on NCUA's review of the written materials. The credit union can then decide whether to move forward with the often expensive, labor intensive conversion process with a full and complete understanding of NCUA's position. NCUA believes its review of these materials is a practical and unintrusive way of fulfilling, at least part of, its congressionally mandated responsibility to review the methods and procedures of the vote to ensure that all reasonable measures to accomplish full disclosure and transparency have been taken to inform the credit union membership of the potential consequences of their vote.

If NCUA disapproves of the methods and procedures of the member vote, after the vote is conducted, then NCUA is authorized to direct a new vote be taken. 12 CFR 708a.7. NCUA interprets its responsibility to review the methods and procedures of the member vote to include determining that the member notice and other materials sent to the members are accurate and not misleading, that all required notices are timely, and that the membership vote is conducted in a fair and legal manner.

NCUA believes that full and proper disclosure to members that they could potentially lose their ownership interest in their credit union if it ultimately becomes a stock institution is key to describing the purpose and subject matter of the member vote adequately. Failing to discuss this integral risk associated with the conversion adequately is tantamount to providing misleading information. Most of the conversion packets NCUA has reviewed since CUMAA went into effect have contained some information relating to this issue, but have not addressed it sufficiently to make this point clear to members.

A charter conversion is a sophisticated transaction with consequences that might not surface for a number of years and that are often not

recognizable at the time of conversion to even the most astute members. As a result, few members can make a truly informed decision about how the conversion will affect their ownership interest in the credit union unless the credit union provides them with this information. Accordingly, for the reasons discussed above and in an effort to achieve full disclosure and transparency, NCUA proposes to require a converting credit union to disclose that the conversion from a credit union to a mutual savings bank could lead to members losing their ownership interests in the credit union if the mutual savings bank subsequently converted to a stock institution and the members do not become stockholders.

The Act provides that a member of a Federal credit union is entitled to only one vote irrespective of the number of shares held by that member. The "one member one vote" structure gives an equal voice to all members, even those of modest means. 12 U.S.C. 1760. Most, if not all, state credit unions also are required to follow this approach. This is not usually the case with mutual savings banks. In most instances, mutual savings banks allot votes based on the amount of a member's deposits. Commonly, one vote is granted for each \$100 a member has on deposit up to a maximum of 1,000 votes. As noted above, NCUA believes that disclosing that members could have lesser voting power in the mutual savings bank than they do in the credit union is central to describing the purpose and subject matter of the member vote in an adequate and proper fashion.

Accordingly, for the reasons discussed above and in an effort to achieve full disclosure and transparency, NCUA proposes to require a converting credit union to disclose that the conversion from a credit union to a mutual savings bank could lead to members having lesser voting rights in the mutual savings bank than they had in the credit union.

NCUA's conversion rule echoes CUMAA by providing that directors and senior management officials of a credit union may not receive any economic benefit from the conversion of their credit union other than compensation and benefits paid to them in the ordinary course of business. 12 CFR 708a.10. This is intended to insure that management's decision to begin the conversion process is based on sound business judgment reflecting the best interests of the members. Consistent with this statutory and regulatory limitation, NCUA believes it is appropriate to require a converting credit union to disclose in the member