



September 15, 2006

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, N.W.
Washington D.C. 20552

Attention: No 2006-29

Re: Stock Benefit Plans in Mutual to Stock Conversions and Mutual Holding Company Structure, 71 FR 41179 (July 20, 2006)

Dear Sir or Madam:

America's Community Bankers ("ACB")¹ welcomes the opportunity to comment on the proposal issued by the Office of Thrift Supervision ("OTS") to clarify its regulations regarding stock benefit plans established after mutual-to-stock conversions or in mutual holding company ("MHC") structures.² The proposal would clarify the current regulations and restrictions, reduce regulatory burden by reorganizing the applicable provisions, and make changes that would eliminate the need for mutual holding companies to seek a waiver of certain requirements.

ACB Position

ACB supports the proposal to make technical amendments to the mutual and mutual holding company regulations. We agree that the clarifications will reduce the regulatory burden on mutual holding companies. We also support the proposal that would reduce the voting requirements for the adoption of stock benefit plans in mutual holding companies. The proposal would reduce the voting requirements for certain stock benefit plans of mutual holding companies, if the plan were adopted more than one year after the issuance of the minority shares. The benefit plan could be adopted on a vote of the majority shareholders, including the mutual holding company.

¹ America's Community Bankers is the national trade association committed to shaping the future of banking by being the innovative industry leader strengthening the competitive position of community banks. To learn more about ACB, visit www.AmericasCommunityBankers.com.

² 71 Fed. Reg. 41179 (July 20, 2006)

Over 90 percent of mutual institutions chartered in the United States, including those in a mutual holding company structure, are members of ACB. We strongly support the ability of management and members of the boards of directors of mutual institutions to make decisions regarding whether the institutions should convert to stock or form a mutual holding company. ACB has a long held policy position that the conversion process should be as rational as possible and we appreciate the OTS's efforts to ensure that the regulations reflect the changes in the market over the years. We appreciate the OTS's support for the mutual form of organization, mutual holding companies and their stakeholders. We support the mutual holding company as an option for mutuals that want to have some corporate flexibility and have the ability to raise capital while retaining their independence.

Mutual community banks and mutual holding companies play a vital role in their communities. The opponents of this proposal are not interested in the ongoing viability of these institutions in their communities. ACB is concerned that in some situations minority shareholders are attempting to exercise control over the MHC in an effort to force the sale of the institution. While minority shareholders cloak these actions under a "good corporate governance" label, all too often their goal is personal enrichment.

ACB believes that shareholder value is maximized by enabling the employment of management who can lead the institutions with services to the community and with new ideas for products and services. If minority shareholders control the policies of a mutual institution, we believe that mutual institutions may not be able to avail themselves of regulatory provisions that allow stock-based compensation for officers and directors as an employee attraction and retention tool.

The benefit plans that are in place at mutual holding companies are restricted as to size and the shareholder dilution is not significant when benefit plans are adopted. The OTS has issued detailed restrictions and requirements regarding stock benefit plans that will still be in place after adoption of this proposed rule.

Finally, the directors of mutual holding companies that will be voting on behalf of the majority mutual holding company for the benefit plans have a fiduciary duty to the shareholders, to the depositors and to the other stakeholders of the company. In approving an appropriate plan that will result in benefits to the institution, they are exercising this fiduciary duty. In addition, OTS requires all boards to annually review compensation arrangements for regulatory and competitiveness concerns.³

Background

The mutual holding company structure was developed in the late 1980's to accommodate the needs of mutual institutions that had no other way to raise capital but did not want to abandon the mutual form of ownership. The first mutual holding company regulations were developed by the OTS in the early 1990's and then were revised in 1994 along with the rules pertaining to mutual

³ OTS Regulatory Bulletin 27b (June 13, 2001), citing 12 C.F.R. Part 570, which prohibits excessive compensation.

to stock conversions. In 2000 and again in 2002, the OTS revised its mutual holding company regulations to provide a more updated approach to the structure, organization and governance in an effort make the mutual holding company a more viable, long-term alternative for mutual institutions seeking additional operational flexibility but not wishing to convert to stock form.

The mutual holding company organizational structure is different from a mutual savings institution or a converted institution in a holding company. It is hard to rationalize the rules and regulations in every respect, but over the years the OTS has worked to develop a regulatory regime that imposes the corporate governance principles applicable to other institutions on the unique features of the mutual holding company. The fundamental premise of a mutual holding company is that the holder of the majority interest - the mutual holding company - retains control of the institution and its operations. The mutual holding company represents or embodies the interests of the depositors and other stakeholders of the institution.

The mutual to stock conversion process and the process to form a mutual holding company are the subject of detailed regulations. The requirements have been amended over the years as the market has changed and processes involving corporate governance generally have developed. The conversion regulation and the mutual holding company regulations have evolved over time to provide that the process is as fair as possible to all stakeholders and that insiders are restricted in the benefits they may enjoy.

The changes made to the regulations in 2002 included a provision that permits mutual holding companies to adopt stock benefit plans that are set as if 49 percent of the stock had been issued to minority shareholders, even if a smaller amount of stock had in fact been issued. There were additional limitations added to the benefit plan provisions that were intended to ensure that insiders would not receive a disproportionate share of minority issuances that were for less than 49 percent of the stock.

A mutual holding company that issues minority shares must comply with all of the rules and regulations for a public company including the disclosure and proxy rules established in the federal securities laws. The process is transparent. The mutual holding company is formed only after a conversion process that includes a subscription offering of the minority shares to all eligible depositors and the community. As part of this process, the purchasers of the shares are given disclosures that describe the rights and obligations of the minority shareholders and they can make a choice once they have seen these disclosures not to purchase the stock.

The required disclosures include those that all public companies must provide to their shareholders. This includes the recently adopted disclosures on compensation recently issued by the Securities and Exchange Commission.⁴ In addition the benefit plans are subject the recent changes in accounting for stock options.

⁴ 71 Fed. Reg. 53158 (September 8, 2006)

The Proposal

The proposal makes a number streamlining and clarifying changes to the benefit plan provisions of the conversion and mutual holding company regulations, including:

- The language of the regulation would be amended to refer to the names of the types of the plans rather than their status as tax qualified plans;
- Reorganization of several applicable provisions of the conversion regulations to the mutual holding company regulations so that it is clear which provisions are applicable;
- Clarification that substantive and procedural requirements in the conversion regulations are applicable to the issuance of minority shares by a mutual holding company, unless the OTS finds they are inapplicable;
- Relocating the language that states that for purposes of the provisions in the rules governing benefit plans “conversion” refers to minority stock issuance;
- Clarification that for purposes of benefit plans established by mutual holding companies, the limitations on the size of the plans is found in the mutual holding company regulations;
- Clarification that each issuance of minority stock would begin a one year period;
- Specifically stating that the limitations on the sizes of the plans and restrictions found in the conversion regulations are applicable to the issuance of minority shares by mutual holding companies; and
- Clarification that certain limitations exist when a plan has been adopted more than one year after the issuance of minority shares.

ACB supports each of these changes. We believe that reorganizing the regulations to include the provisions applicable to mutual holding companies in the same place is beneficial for mutual holding companies that are working with the requirements.

Maximum Purchase Limitations

Finally, the OTS is proposing to increase the options available regarding the maximum purchase limitations available for subscriptions in mutual to stock conversions. Currently, a converting association is permitted to establish a maximum purchase limitation between one and five percent of the amount of the stock sold. The proposal would permit a converting association to establish a maximum purchase limitation that is under one percent.

ACB supports this proposed change. It is appropriate to allow an institution that wishes to further restrict the maximum amount of shares that may be purchased in a conversion to do so free of the regulatory burden of seeking a waiver of the current requirement.

Proposal to Amend the Vote Requirement for Benefit Plans of Mutual Holding Companies

The OTS also proposes to revise the regulation to require a vote of the minority shareholders on a benefit plan of a mutual holding company only during the first year after a minority offering.

The agency also proposes to revise the provision to require approval (during the first year after a minority stock issuance) by a majority of the minority shares voting on the adoption of the plan, rather than the majority of the outstanding shares.

The OTS's mutual to stock conversion regulations permit a converted institution to adopt a stock option plan or other employee benefit plan within 12 months of the conversion, if a number of procedural and substantive requirements are met, including that the shareholders must approve the plan by a majority of the total votes eligible to be cast at a duly called meeting before the establishment of the plan. The current regulation also states that if the converted institution is a subsidiary of a mutual holding company, a majority of the total votes eligible to be cast (other than the parent mutual holding company) must approve each plan before the establishment or implementation of the plan.⁵

The OTS chief counsel issued an interpretive opinion on September 17, 2004⁶ confirming that the requirements governing the approval of stock benefit plans established in full conversions are applicable to the benefit plans established in mutual holding company formations. The letter says that these requirements are applicable no matter how much time has elapsed from the initial issuance of stock. The letter further says that the OTS will grant waivers of these requirements on a case by case basis. In practice, the OTS routinely grants a waiver of the current voting requirement.

The proposal would eliminate the necessity for a mutual holding company adopting a benefit plan to apply for a waiver. Not only would this action reduce regulatory burden but it would also reduce the uncertainty that can arise when a waiver of any regulation must be requested.

The ability of mutual holding companies to offer stock-based compensation to their officers and directors in a manner more in line with what is available for stock institutions is important to their ability to attract and retain qualified employees. Benefit plans play an important role in ensuring high quality management team.

While the provisions related to benefit plans were updated to reflect the market, the regulation continues to require that certain safeguards regarding the adoption and approval of these plans be in place. The regulation and the model charters for mutual holding companies and mid tier mutual holding companies do not contemplate that minority shareholders will control the votes on the benefit plans.

Mutual holding companies that have issued minority shares are subject to the same disclosure and reporting requirements applicable to other public companies. The shareholders who purchase minority shares are informed of their rights and the limitations of their ownership prior to purchasing the shares. Minority shareholders who purchases shares in the subscription or

⁵ 12 CFR 563b.500

⁶ Letter from John Bowman, OTS Chief Counsel dated September 17, 2004 (P-2004-6)

community offerings likely remain depositors in the institution. They have an interest in ensuring that the mutual holding company investment provides shareholder value, but they have a broader interest in ensuring that the institution remains a viable and healthy community bank.

To the extent that the benefit plans are adopted one year or more after the issuance of minority stock, the proposal would permit the majority of the shareholders to approve the plan. The majority holder of the stock can adopt the benefit plan, just as any majority owner of stock in any public company. The directors of the majority owner have a fiduciary duty that extends to the depositors of the institution as well as to the minority shareholders. They are obligated to follow the general principles of good corporate governance and to adopt benefit plans that satisfy standards of diligence and loyalty that are applicable to them. Moreover, OTS requirements and regulations prohibit excessive compensation and require boards of directors to monitor compensation.

ACB appreciates the opportunity to comment on this important matter. Should you have any questions about this letter please contact, Patricia Milon at (202 857 -3121) or pmilon@acbankers.org.

Sincerely,

A handwritten signature in black ink, appearing to read "Patricia Milon". The signature is fluid and cursive, with a long horizontal flourish extending to the right.

Patricia A. Milon
Chief Legal Officer and Senior Vice President,
Regulatory Affairs