11-4

May 13, 2011

Re: Conversion of a California State Chartered Credit Union to a Federal Mutual Savings Bank

Dear Mr. _____:

This responds to your letter of April 27, 2011, whereby you argue that California's '"state chartering law permits . . . [a California state chartered credit union] to convert to a mutual savings and bank . . . ."'

In support of your argument, your letter provides reasoning that combines the ability of a credit union to enter into a purchase and assumption agreement with a federal mutual savings bank with the powers granted a credit union under the California Non Profit Mutual Benefit Law (Corporations Code Section 7110, et seq.). We agree with that reasoning. It is our opinion that a California state chartered credit union may convert to a federal mutual savings bank in the manner described in your letter. Furthermore, we agree with your statement that "It is understood that if any California law requirements relating to the P&A and resulting conversion to a mutual savings bank (including but not limited to any internal corporate governance requirements, such as the requisite membership vote for conversion and the determination of a member's eligibility to vote) are more stringent than those applicable under the FCUA and the regulations of the NCUA, the more stringent requirements will prevail."

Please be advised that our agreement with your argument regarding the conversion of California state-chartered credit unions to federal mutual savings banks as set forth in your letter should not be seen as a statement that there is only one way to convert a California state-chartered credit union to another financial institution charter. There may be other avenues used to convert a credit union into another form of financial institution. However, such other methods are not before us for determination at this time.

I trust this has been responsive to your request. Please feel free to contact me at (916) 322-1570 if you have any questions or comments regarding this letter.

Sincerely,

Kenneth Sayre-Peterson
Acting General Counsel

KSP:pjp

April 27, 2011

BY FEDERAL EXPRESS

Kenneth Sayre-Peterson
Acting General Counsel
California Department of Financial Institutions
1810 13th Street
Sacramento, California 95811

Re: Conversion of a California Credit Union to a Federal Mutual Savings Bank

Dear Mr. Peterson:

As you are aware, if a credit union incorporated under the California Credit Union Law, Div. 5 of the California Financial Code, §§ 14000 *et seq.* (California Credit Union) that is insured by the National Credit Union Insurance Fund and regulated by the National Credit Union Administration (NCUA) wishes to convert to a mutual savings bank, it must comply with the applicable provisions of California law and with the Federal Credit Union Act (FCUA) and the regulations of the NCUA thereunder, as well as the requirements of the Federal Deposit Insurance Corporation and the relevant chartering agency. The NCUA's regulations applicable to such a conversion include a requirement that is to be codified as 12 C.F.R. § 708a.105(a)(3)[1] that a state-chartered credit union must include in its notice to the NCUA concerning the conversion a statement as to whether "its state chartering law permits it to convert to a mutual savings bank and provide the specific legal citation."

We believe that California law permits a California Credit Union to convert to a federal mutual savings bank in the manner described below, which, except to the extent (if any) that the regulations of the NCUA on conversion of credit unions (12 C.F.R. Part 708a) expressly provide more stringent requirements, would be subject to the requirements of applicable California law and the charter and bylaws of the credit union with respect to corporate governance of the credit union, the eligibility of credit union member to vote on the transaction, the conduct of the meeting of credit union members to vote whether to approve the transaction, and the requisite vote for member approval. We request that you issue an opinion to this effect.

The California Credit Union Law does not include an explicit provision authorizing such a conversion. However, as explained below, it does include authority for a California credit union to engage in a purchase and assumption transaction with a federal mutual savings bank by which it would transfer all (or substantially all) of its assets and liabilities to the federal mutual savings bank (P&A). The federal mutual savings bank would assume the share accounts of the California credit union members and the loans made by the California credit union, as well as the

[1] 75 Fed. Reg. 81378 (Dec. 28, 2010).

other assets and liabilities of the credit union. The deposit accounts of the federal mutual savings bank would be insured by the FDIC. Upon consummation of the P&A, the former members of the credit union would have voting rights in the federal mutual savings bank. Thus, in the case of a P&A with a *de novo* shell federal mutual savings bank established to facilitate the transaction, the result would be functionally the same as if a direct conversion to a federal mutual savings bank had occurred.

Although the California Credit Union Law include explicit authority for a California Credit Union to merge only with another credit union or corporate credit union (§ 15200) and to convert directly only into a federal credit union (§ 15300), it provides in § 14052 that "[i]n addition to the powers enumerated by this division [i. *e.*, the California Credit Union Law], every credit union has the general powers conferred upon corporations by the Nonprofit Mutual Benefit Corporation Law of this state unless restricted by this division." Section 14002.5 is the only section of the California Credit Union Law that restricts application to a California credit union of the general powers conferred on corporations by the Nonprofit Mutual Benefit Corporation Law.

Under subdivision (a) of §14002.5, "all provisions of law applicable to nonprofit mutual benefit corporations generally including, but not limited to, the Nonprofit Mutual Benefit Corporation Law (Part 3 (commencing with Section 7110) of Division 2 of Title I of the Corporations Code)) shall apply to credit unions. However, whenever any provision of this division [the California Credit Union Law] applicable to credit unions is inconsistent with any provision of law applicable to nonprofit mutual benefit corporations generally, the provisions of this division shall apply and the inconsistent provision of law applicable to nonprofit mutual benefit corporations generally shall not apply to a credit union." Subdivision (b) goes on to provide that, notwithstanding subdivision (a), certain specified provisions of the Corporations Code are not applicable to California credit unions. None of those specified provisions has any relevance to the question of whether a California credit union may engage in a P&A.

The Nonprofit Mutual Benefit Corporation Law includes §7911 (titled "Principal terms of sale; Abandonment of proposed transaction) of the Corporations Code, which provides that:

> (a) Subject to the provisions of Section 7142, a corporation may sell, lease, convey, exchange, transfer or otherwise dispose of all or substantially all of its assets when the principal terms are:
>
> (1) Approved by the board; and
>
> (2) Unless the transaction is in the usual and regular course of its activities, approved by the members (Section 5034), either before or after approval by the board and before or after the transaction.
>
> (b) Notwithstanding approval by the members (Section 5034), the board may abandon the proposed transaction without further action by the members, subject to the contractual rights, if any, of third parties.
>
> (c) Subject to the provisions of Section 7142, such sale, lease, conveyance, exchange, transfer or other disposition may be made upon such terms and conditions and for such consideration as the board may deem in the

> best interests of the corporation. The consideration may be money, property, or securities of any domestic corporation, foreign corporation, or foreign business corporation or any of them.

Clearly, this authority permits a purchase and assumption transaction. The transaction would be subject to § 7142, but that section applies only to a corporation holding assets in charitable trust, which is not relevant here. Section 7911 references § 5034 with respect to approval of a transaction by the members. Section 5034 defines "approval by the members" as:

> approved or ratified by the affirmative vote of a majority of the votes represented and voting at a duly held meeting at which a quorum is present (which affirmative votes also constitute a majority of the required quorum) or written ballot in conformity with Section 5513, 7513, or 9413 or by the affirmative vote or written ballot of such greater proportion, including all of the votes of the memberships of any class, unit, or grouping of members as may be provided in the bylaws (subdivision (e) of Section 5151, subdivision (e) of Section 7151, or subdivision (e) of Section 9151) or in Part 2, Part 3, Part 4 or Part 5 for all or any specified member action.

We do not believe that the provisions of the Nonprofit Mutual Benefit Corporation Law described above that apply to a purchase and assumption transaction are in any way inconsistent with the provisions of the California Credit Union Law. The California Credit Union Law does not speak to purchase and assumption transactions directly, but by incorporating the powers of a nonprofit mutual benefit corporation into the powers of a California Credit Union, the California Credit Union law provides to a California credit union proposing to engage in a P&A a power similar to that granted to other depository institutions chartered under California law (a bank, savings association or industrial loan company) under Div. 1.5 of the Financial Code to engage in a sale of a whole business unit, *i.e.*, all or substantially all of the business of a depository corporation (§4840(i) of the Financial Code).

Accordingly, we believe that a California credit union is authorized by California law to enter into a P&A. It is understood that if any California law requirements relating to the P&A and resulting conversion to a mutual savings bank (including but not limited to any internal corporate governance requirements, such as the requisite membership vote for conversion and the determination of a member's eligibility to vote) are more stringent than those applicable under the FCUA and the regulations of the NCUA, the more stringent requirements will prevail.

We look forward to your response to our request.

Yours truly,