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Credit union's deal for tiny thrift has mutual bank advocates on edge

By John Reosti
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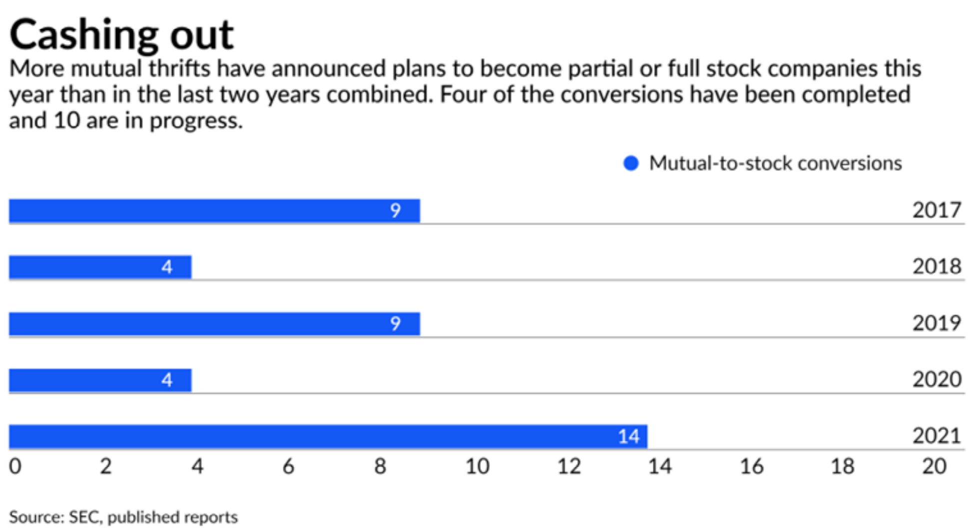
The case of a one-branch thrift selling itself to Minnesota's largest credit union has mutual banking advocates lining up in opposition out of fear it's a bad omen for depositor-owned institutions.

At issue is the $72.5 million-asset Brainerd Savings & Loan in Minnesota, which agreed to be sold to the $7.2 billion-asset Wings Financial Credit Union in Minneapolis in January.

A growing number of mutuals are selling shares to investors and converting to stock ownership through second-step mutual holding company offerings, or through full mutual-to-stock conversions. So far this year, 13 mutual institutions have announced or completed second-step or full-conversion transactions. One other mutual has completed a first-step sale of a minority stake to investors.

In 2020, a total of four depositor-owned banks pursued stock sales.



Since credit unions lack the authority to buy mutuals directly, Brainerd plans to liquidate, sell its assets to Wings and then distribute proceeds among its depositor-owners.

Banking trade groups, including the Independent Community Bankers of America, America's Mutual Banks and the American Bankers Association, have called on the Office of the Comptroller of the Currency, Brainerd's primary regulator, to kill the deal by rejecting the thrift's application to terminate its charter.

"They're getting around the merger issue by dissolving the [bank] and buying the assets, which is essentially merging" the two institutions, said Chris Cole, executive vice president and senior regulatory counsel at ICBA.

“We’re very concerned this will accelerate the decline of mutuality for banks,” Cole said. Mutual banks “already have enough challenges with the pandemic and their net interest margins. This is not helping them.”

Banker groups complained further that Brainerd and Wings have declined to release key details of the deal — including the price Wings is paying and any sums Brainerd executives might receive — claiming the unusual structure exempts them from complying with merger-related disclosure rules.

“The critical components of who gets what and how this is going to be executed are basically hidden from the public,” said Douglas Faucette, a partner with Locke Lord in Washington.

“It’s critical that the OCC, if it determines to approve this, makes public the reasons,” said Faucette, who is a director at America’s Mutual Banks. “You have a comprehensive scheme that subjects almost everything that involves the governance of a mutual to strict regulatory scrutiny. … But, gee, you can [purchase and assume] all the assets of a mutual and pay out the residue to the members. That’s a rubber stamp. It was just routinely approved in the field.”

“It’s really unusual to dissolve a mutual to do this kind of transaction,” Cole said.

The ICBA and America’s Mutual Banks submitted a joint comment letter to the OCC criticizing the Wings-Brainerd transaction earlier this month. American Bankers Association President and CEO Rob Nichols submitted his own comment letter April 20.

According to Nichols, smoothing the way for the voluntary liquidation of a healthy mutual bank would tempt depositors and management to liquidate institutions to release that value, to the detriment of banking services in the institutions' communities.

“It is not in the public interest to see institutions vanish to distribute the accumulated earnings of years of sound, profitable operations,” Nichols said in his letter.

Brainerd has struggled to break even in recent years. It reported net income of $7,000 in the first quarter after losing a combined $1 million from 2017 to 2020. The company’s most recent annual profit, totaling $95,000, came in 2016.

At the same time, Brainerd remained well capitalized and reported virtually no problem loans on its first-quarter call report with the Federal Deposit Insurance Corp.

Spokesmen for both Brainerd and Wings had not responded to a request for comment at deadline.

The proposed combination involving Brainerd and Wings “has profound policy implications,” said Thomas Fraser, president and CEO of the $2.4 billion-asset First Mutual Holding Co. in Lakewood, Ohio. “It’s overturned what was settled policy and procedure for the past 50 years.”

“This touched a raw nerve with almost every mutual banker I’ve talked with,” Fraser said.

Fraser has established himself as a leading advocate for mutuals. He created First Mutual in 2015 to bring depositor-owned banks together under a common umbrella, allowing them to share administrative, compliance and technology costs. First Mutual has acquired five affiliate banks, including First Federal Lakewood, the bank Fraser ran from 2013 to 2018.

Despite his efforts to preserve mutuals, Fraser said he has no concerns over the growing number of mutual-to-stock conversions.

“I think it’s up to every mutual bank to figure out the right path forward, but it’s got to be 100% in compliance with law policy and regulation,” Fraser said. “It shouldn’t be novel, and the depositor interest has got to be protected and paramount throughout.”

Stock sales by mutual banks are likely to continue during the second half of 2021 and into 2022, said Kip Weissman, a partner at Luse Gorman in Washington.

“There are definitely discussions going on,” Weissman said. “Mutual or stock, if you’re under $50 billion of assets, you’re probably looking around and thinking, What can I do to make my bank more relevant? … Capital is a good way to start.”

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