

OFFICE OF THRIFT SUPERVISION

Approval of Conversion of a State Savings Bank to a Federal Savings Bank, Holding Company Applications, Waiver Request and Related Filings

Order No.: 2004-20

Date: April 23, 2004

Docket Nos.: H-4021, H-4099, and 17968

Westfield Bank, Westfield, Massachusetts (Savings Bank) has filed an application to convert from a Massachusetts-chartered savings bank to a federal savings bank, pursuant to 12 C.F.R. § 552.2-6. Westfield Mutual Holding Company (State MHC), the Savings Bank's state-chartered mutual holding company, has applied to convert, in a two-step transaction, to a federal mutual holding company (Federal MHC). The application requests that the Office of Thrift Supervision (OTS) waive 12 C.F.R. § 575.14(c), which requires a subsidiary holding company to have a federal charter, in order to allow the Savings Bank's current mid-tier mutual holding company, Westfield Financial, Inc. (Stock Holding Company) to retain its Massachusetts charter. (Collectively, the Savings Bank, State MHC, and Stock Holding Company are referred to as "Applicants.")

In addition, the Federal MHC and the Stock Holding Company have requested OTS approval under 12 U.S.C. § 1467a(e) and 12 C.F.R. §§ 574.3 and 575.14 to acquire the Savings Bank. The application also includes a notice for the establishment of an operating subsidiary under the OTS Subordinate Organizations Regulations, 12 C.F.R. Part 559, and for approval of the subsidiary and its activities, pursuant to 12 C.F.R. § 575.11.

The Proposed Transaction

The Savings Bank proposes to convert directly from a state-chartered savings bank to a federal savings bank. The State MHC proposes to convert to a federal charter by chartering the Federal MHC and then merging into it. The Stock Holding Company will remain a Massachusetts chartered stock holding company, which will become a savings and loan holding company owning all of the Savings Bank's stock.

Conversion of the Savings Bank to a Federal Charter

Section 552.2-6 of OTS' regulations provides that, with OTS approval, any stock depository institution that is, or is eligible to become, a member of a Federal Home Loan Bank, may convert to a federal stock savings association, provided that the depository institution, at the time of conversion, has deposits insured by the Federal Deposit Insurance Corporation, and the depository institution, in accomplishing the conversion, complies with all applicable statutes and regulations. The resulting federal savings

association must comply within the time prescribed by OTS to the requirements of section 5(c) of the Home Owners' Loan Act (HOLA).

The proposed conversion of the Savings Bank conforms to the requirements of section 552.2-6. The Savings Bank is a state-chartered, Bank Insurance Fund (BIF)-insured savings bank, with membership in a Federal Home Loan Bank. The Savings Bank has certain equity investments that are impermissible for a federal stock savings bank, and has requested that it be permitted to retain those investments for up to two years after the proposed conversion. OTS is imposing a condition requiring that the Savings Bank divest the impermissible equity investments within two years after consummation of its conversion to a federal charter.

The HOLA provides that OTS may grant a federal savings association charter only: (i) to persons of good character and responsibility; (ii) if, in OTS' judgment, a necessity for such savings association exists in the community to be served; (iii) if there is a reasonable probability of the association's usefulness and success; and (iv) if the association can be established without undue injury to properly conducted existing local thrift and home financing institutions.¹ OTS regulations include the same standards, with the additional requirement that OTS consider whether the association will promote credit for housing consistent with the safe and sound operation of a federal savings association. In addition, OTS' Community Reinvestment Act (CRA) regulations provide that an applicant for a federal thrift charter must submit with its application a description of how it will meet its CRA objectives and that OTS may deny or condition approval of the application on CRA grounds.²

With respect to character and responsibility, the Savings Bank's management, and that of its holding companies, will not change in connection with the subject transaction. The Savings Bank's management, which includes the same individuals as the management of its holding companies, is well-rated. OTS concludes that the character and responsibility of the organizers of the Savings Bank are consistent with approval.

As for the two standards regarding the necessity for the Savings Bank in the community, and undue injury to properly conducted existing local thrift and home financing institutions, the Savings Bank will continue its current business activities. Accordingly, OTS concludes that there is a necessity in the community for the Savings Bank, and that the existence of the federal savings bank will not result in harm to existing institutions.

Based on the Savings Bank's business plan, historical data regarding the Savings Bank, the Savings Bank's proposed capital levels, and competence of management, OTS concludes that there is a reasonable probability of the Savings Bank's usefulness and success.

¹ 12 U.S.C. § 1464(e).

² 12 C.F.R. § 563e.29(b) (2003).

Based on the Savings Bank's plans to engage in mortgage lending to a significant extent, as well as the Savings Bank's business plan and management experience, OTS concludes that the Savings Bank's role in providing credit for housing consistent with safe and sound operations of a federal association is consistent with approval.

OTS reviewed the Savings Bank's plan for compliance with the CRA and the results of the Savings Bank's most recent compliance examination. OTS received no comments objecting to the application on CRA grounds. Accordingly, OTS concludes that approval of the charter conversion is consistent with the CRA.

Conversion of the State MHC to the Federal MHC

The subject application contemplates the conversion of the State MHC to the Federal MHC. The proposed structure of the transaction, including but not limited to the formation of the Federal MHC, and the merger of the State MHC into the Federal MHC, is consistent with the OTS MHC regulations. The merger of the State MHC into the Federal MHC is contemplated under 12 C.F.R. § 575.10(a)(3). The Federal MHC's charter is consistent with 12 C.F.R. § 575.9. The Stock Holding Company proposes to hold all of the common stock of the Savings Bank, as required under 12 C.F.R. § 575.14(a).

Regulatory Waiver

The Applicants have requested that OTS waive 12 C.F.R. § 575.14(c) to permit the Stock Holding Company to retain its state charter, instead of becoming a federally chartered subsidiary holding company.

OTS regulations, at 12 C.F.R. § 500.30(a), provide that OTS may, for good cause and to the extent permitted by statute, waive the applicability of any provision of OTS' regulations. No statute requires that a mid-tier holding company have a federal charter.

In the preamble to the final rule adding provisions regarding subsidiary holding companies to OTS' MHC regulations, OTS set forth several reasons for requiring subsidiary holding companies to have a federal charter.³ OTS stated that requiring subsidiary holding companies to be federally chartered is consistent with Congressional intent regarding mutual holding companies, because it provides a clear regulatory framework for the regulation of mutual holding companies. OTS also intended to ensure that it would be able to effectively protect the rights of the mutual holding company's mutual members and ensure consistent treatment under the OTS mutual to stock conversion regulations for mutual members of mutual holding companies and members of mutual associations that do not form mutual holding companies. OTS also was concerned that permitting the establishment of state-chartered subsidiary holding

³ See, 63 FR 11361 (Mar. 9, 1998), at 11361 – 11362.

companies would diminish OTS' ability to regulate the corporate governance provisions of subsidiary holding companies. Also, OTS stated that by requiring the subsidiary holding company to be federally chartered, its authority in receivership situations under section 10(o)(9) of the HOLA was clearer.

With respect to the first point mentioned in the previous paragraph, OTS can, in many situations, address its regulatory concerns regarding subsidiary holding companies through the MHC regulations and the general provisions of section 10 of the HOLA regarding savings and loan holding companies even where the subsidiary holding company is state-chartered.

OTS believes, however, that it is necessary to ensure that it has absolute authority regarding the subsidiary holding company in connection with any stock issuance by the subsidiary holding company, and in connection with any mutual to stock conversion by the mutual holding company. Accordingly, OTS is conditioning its grant of the waiver request on the requirement that, before the Stock Holding Company issues any additional stock, and before the Federal MHC converts to stock form, the Stock Holding Company must convert to a federal charter.

The condition not only addresses the first reason for the requirement for a federal charter, discussed above (clear regulatory authority), but addresses the second and third reasons as well, that is, protection of the mutual holding company's mutual members, and ensuring consistent treatment of members of a converting mutual holding company and members of a converting savings association. OTS has broad authority to condition any waiver of its regulations.

With respect to the next reason that OTS imposed the federal charter requirement, ability to regulate the corporate governance provisions of the subsidiary holding company, OTS is conditioning approval of the waiver on the Stock Holding Company complying with the indemnification provisions of 12 C.F.R. § 575.11(f) as if it were a federally chartered company, and obtaining OTS approval within two years of the date of this Order for any provision of the Stock Holding Company's charter or bylaws that is materially different from the federal subsidiary holding company charter or bylaw provisions contained in or referenced in 12 C.F.R. § 575.14(c), and obtaining prior OTS approval of any amendment to the Stock Holding Company's charter and bylaws, after the date of this Order, where the terms of the amendment are materially different from the federal subsidiary holding company charter or bylaw provisions contained in or referenced in 12 C.F.R. § 575.14(c). These conditions help ensure that the Stock Holding Company's corporate governance provisions do not undermine the regulatory structure envisioned in Part 575. These conditions are particularly appropriate where, as here, the boards of directors of the top-tier mutual holding company, the subsidiary holding company, and the savings association have substantial overlaps.

The federal charter requirement also was imposed to ensure that OTS' authority was clear in the context of a receivership situation, in which prompt regulatory action is

often essential. In this case, the Stock Holding Company's only significant asset is the stock of the Savings Bank, and the Federal MHC's only significant asset will be stock of the Stock Holding Company. In such a situation, OTS' clear authority regarding the top-tier mutual holding company and the depository institution should be sufficient to ensure that OTS' regulatory interests are met. OTS has sufficient regulatory authority, for example, with respect to dividends and mutual holding company activities, to ensure that appropriate measures are in place before the Stock Holding Company acquires a significant amount of assets other than the stock of the Savings Bank.

In the current situation, the Savings Bank is already controlled by the State MHC and the Stock Holding Company. Such a situation is distinguishable from a situation in which the depository institution is undergoing its initial mutual holding company reorganization. Applicable regulators already have experience with the Savings Bank's existing holding companies, and the reorganization was approved under applicable state law. Also, the conversion of the existing state-chartered subsidiary holding company involves expenses that are not encountered in an initial mutual holding company reorganization.

Finally, OTS is conditioning approval of the waiver request on the requirement that the Stock Holding Company be subject to 12 C.F.R. § 575.14(a). This provision requires that a subsidiary holding company hold all of the stock of the subsidiary savings association, and states that the subsidiary holding company may not be used as a means to evade part 575 or part 563b. This requirement will help ensure that the rights of the Federal MHC's mutual members are not undermined, and that the purposes of parts 575 and 563b are fulfilled.

Based on the foregoing, OTS concludes that there is good cause to waive 12 C.F.R. § 575.14(c) to permit the Stock Holding Company to have a state charter, subject to the above-described conditions.

Holding Company Application

In the proposed transaction, the Federal MHC and the Stock Holding Company would acquire the Savings Bank. Accordingly, the transaction requires OTS approval under Section 10(e) of the HOLA, and the OTS regulations thereunder (Control Regulations).

Section 10(e)(1)(B) of the HOLA and the Control Regulations provide that the OTS must approve a holding company application proposing the acquisition of a savings association by a company other than a savings and loan holding company, unless the OTS finds the financial and managerial resources and future prospects of the company and association involved to be such that the acquisition would be detrimental to the savings association or the insurance risk of the Savings Association Insurance Fund or

BIF.⁴ OTS must consider the impact of any acquisition on competition.⁵ In addition, 12 C.F.R. § 563e.29(a) requires that OTS take into account assessments under the CRA when approving holding company applications.

As for managerial resources, for the reasons set forth in the discussion of the Savings Bank's charter conversion, OTS concludes that the Savings Bank's managerial resources are consistent with approval. The board of directors of the Federal MHC and the Stock Holding Company will continue to consist of the present directors of the Savings Bank. Accordingly, OTS concludes that the managerial resources of the Federal MHC and the Stock Holding Company are consistent with approval.

As for financial resources, the Savings Bank's core and total risk-based capital ratios were 10.18 percent and 19.57 percent, respectively, as of December 31, 2003. The Savings Bank will continue to be well-capitalized upon consummation of the transaction. The only activity of the Federal MHC will be its majority ownership of the stock of the Stock Holding Company, and the only activity of the Stock Holding Company will be ownership of the stock of the Savings Bank. Accordingly, OTS concludes that the financial resources of the Federal MHC, the Stock Holding Company, and the Savings Bank are consistent with approval.

After considering the financial and managerial resources of the Applicants and the Savings Bank's business plan, OTS concludes that the future prospects of the Applicants, and risks to the BIF, are consistent with approval.

The proposed acquisition will not cause the Savings Bank to become affiliated with any other operating depository institution. Accordingly, the transaction is not objectionable on competitive grounds.

As for the CRA, the Savings Bank currently has a Satisfactory CRA rating. OTS has received no comments objecting to the proposed transaction. Accordingly, OTS concludes that approval of the holding company application is consistent with the CRA.

Subsidiary

The Savings Bank has one active subsidiary, Elm Street Securities Corp. (Operating Subsidiary), a wholly owned subsidiary of the Savings Bank. The Operating Subsidiary engages in buying, selling, holding, and otherwise dealing in securities exclusively for its own account and not as a broker. The Operating Subsidiary only owns, and will only invest in, permissible investments for federal savings associations. We have considered the Operating Subsidiary under the OTS Subordinate Organization regulations,⁶ and have concluded that it meets the relevant regulatory requirements.

⁴ 12 U.S.C. § 1467a(e)(1)(B) and 12 C.F.R. § 574.7 (2003).

⁵ 12 U.S.C. § 1467a(e)(2).

⁶ 12 C.F.R. Part 559 (2003).

Section 575.11(a) requires prior OTS approval of mutual holding company activities, and also provides that a mutual holding company (or its non-savings association subsidiaries) may engage in activities specified in, *inter alia*, 12 C.F.R. § 575.10(a)(6). Permissible investments for a federal savings association under Part 559 are among the investments permitted under 12 C.F.R. § 575.10(a)(6). Section 575.10(a)(6)(ii) provides that a mutual holding company may not hold shares of an entity that is controlled by the mutual holding company's savings association subsidiary.

OTS has concluded that the Savings Bank's proposed operating subsidiary investment in the Operating Subsidiary is permissible for federal associations. With respect to § 575.10(a)(6)(ii), OTS has previously concluded that section 575.10(a)(6)(ii) does not prevent a savings association subsidiary of a mutual holding company from holding a subsidiary, but is intended to prevent certain situations where the mutual holding company and the savings association subsidiary both hold stock of the subsidiary. In this case, the Federal MHC and the Stock Holding Company will own no direct interest in the Operating Subsidiary.

The Operating Subsidiary engages in activities that are permissible for a federal savings association. OTS has previously concluded that savings association investments of the type contemplated by the Savings Bank, where the Federal MHC and the Stock Holding Company will not hold interests in the Operating Subsidiary, other than indirectly through the Savings Bank, are permitted under 12 C.F.R. § 575.10(a)(6)(ii).

Conclusions

Based on the foregoing analysis, OTS concludes that the applications for conversion to federal charters of the Savings Bank and the State MHC, the Federal MHC's and Stock Holding Company's holding company application, the notice for the Operating Subsidiary under 12 C.F.R. Part 559, and the Federal MHC's application under 12 C.F.R. § 575.11(a) meet the applicable approval criteria. Accordingly, the foregoing applications are hereby approved, provided that the following conditions are complied with in a manner satisfactory to the Northeast Regional Director, or his designee (Regional Director):

1. The Savings Bank, the State MHC, and the Stock Holding Company must receive all required regulatory, shareholder, State MHC corporator, and member approvals, prior to consummation of the transaction, with copies of all such approvals supplied to the Regional Director;
2. The proposed transactions must be consummated within 120 calendar days after the date of this Order;
3. The Applicants must submit a final accounting opinion regarding the accounting treatment for the proposed transaction, prepared by an independent auditor or qualified financial officer, prior to consummation of the proposed transaction;

4. On the business day prior to the date of consummation of the proposed transactions, the chief financial officers of the Savings Bank, the State MHC, and the Stock Holding Company, must certify in writing to the Regional Director that no material adverse events or material adverse changes have occurred with respect to the financial condition or operations of the Savings Bank, the State MHC, or the Stock Holding Company, respectively, since the date of the financial statements submitted with the applications. If additional information having a material adverse bearing on any feature of the applications is brought to the attention of the Savings Bank, the State MHC, the Stock Holding Company, or OTS since the date of the financial statements submitted with the applications, the transaction must not be consummated unless the information is presented to the Regional Director, and the Regional Director provides written non-objection to consummation of the transaction;
5. Upon completion of the transaction, all employment agreements of the Federal MHC, Stock Holding Company and Savings Bank, must be approved in writing by the Regional Director before their execution;
6. The Savings Bank must divest the equity investments identified in the application within two years from the date of consummation of the charter conversion; and
7. No later than five calendar days from the date of consummation of the transaction, the Savings Bank, the Federal MHC, and the Stock Holding Company, must file with the Regional Director a certification by legal counsel stating the effective date of the transaction, the exact number of shares of stock of the Savings Bank acquired by the Stock Holding Company, the exact number of shares of the Stock Holding Company acquired by the Federal MHC, and that the transaction was consummated in accordance with all applicable laws and regulations, the applications, the Amended Plan of Charter Conversion, and all representations and commitments made by the Savings Bank and its counsel in connection with OTS' review of the proposed transactions, and this Order.

In addition, OTS concludes that there is good cause to grant the request for a waiver of 12 C.F.R. § 575.14(c) in order to permit the Stock Holding Company to have a Delaware charter, provided that the Stock Holding Company and the Federal MHC comply with the following conditions. Accordingly, the waiver request is hereby approved, subject to the following conditions:

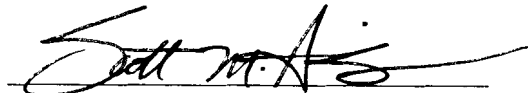
1. The Stock Holding Company must convert to a federal charter prior to the earlier to occur of: (i) any additional issuance of stock by the Stock Holding Company; or (ii) a stock conversion of the Federal MHC;
2. The Stock Holding Company must comply with 12 C.F.R. § 575.11(f) as if it were federally chartered, obtain OTS approval within two years of the date of this Order for any provision of the Stock Holding Company's charter and bylaws that

is materially different from the federal subsidiary holding company charter and bylaw provisions contained in or referenced in 12 C.F.R. § 575.14(c), and obtain prior OTS approval for any amendment to the Stock Holding Company's charter or bylaws, after the date of this Order, where the terms of the amendment are materially different from the federal subsidiary holding company charter or bylaw provisions contained in or referenced in 12 C.F.R. § 575.14(c); and

3. The Stock Holding Company is subject to 12 C.F.R. § 575.14(a) as if it were federally chartered.

Any time period set forth herein may be extended for up to 120 calendar days, for good cause, by the Regional Director.

By order of the Director of the Office of Thrift Supervision, or his designee,
effective April 23, 2004.



Scott M. Albinson
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