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# MHCs Continue to be the Preferred Capital Raising Model for Thrifts

Mutual holding companies (MHCs) continue to be the preferred capital raising structure for savings banks, as MHCs accounted for 9 of the 12 conversion transactions involving the sale of common stock completed to date in 2005. In addition, seven MHC stock offerings, one standard conversion and two MHC "second-step" conversions have either been announced or are pending this year, bringing to 22 the total number of completed or announced deals thus far in 2005. By comparison, 17 MHC stock offerings, three standard conversions and five "second-step" conversions were completed in all of 2004.

Flexibility has been a key to the success of MHCs, and new charter alternatives for federal MHCs have further enhanced the MHC model. Overall, federal MHCs dominated MHC activity in 2004 and 2005. Recently, however, there has been renewed interest in the state-chartered MHC model.

The primary appeal of MHCs continues to be:

- ***Control*** – MHCs preserve the mutual ownership and control of a savings bank.
- ***Better Capital Management*** – MHCs raise less than half the capital of a standard conversion. This reduces the pressure to reinvest new capital quickly and produces a better return on equity.
- ***Dividends*** – MHCs can pay attractive and sustained dividends to stockholders, and federal MHCs are permitted to waive their receipt of dividends.
- ***Stock Benefits*** – MHCs offer the same stock benefits of fully converted stock holding companies without risking a loss of control.

**MHC Charter Flexibility**

One of the most important MHC developments in the past year has been the increased charter flexibility associated with the MHC structure. Today, there are numerous charter alternatives for savings banks considering an MHC, which means more choices to fit the needs of each institution.

The most significant charter development for federal MHCs in 2004 was the OTS decision to allow **Putnam Savings Bank**, Putnam, Connecticut to convert its existing Connecticut savings bank and MHC charters to federal charters and at the same time *retain corporator voting* (rather than depositor voting) in the MHC. This was followed by the MHC reorganization and stock offering by **Georgetown Savings Bank**, Georgetown, Massachusetts, where the savings bank converted to a federal savings bank charter and formed a federal MHC with corporator (instead of depositor) voting. (Our law firm represented **Putnam Savings Bank** and **Georgetown Savings Bank** in these transactions.) The OTS decision in the **Putnam Savings Bank** and **Georgetown Savings Bank** transactions means that state-chartered savings banks that form federal MHCs may retain in the federal MHC the same form of corporate governance that they had in the mutual savings bank immediately prior to the MHC formation.

Another recent MHC charter development is that the OTS now permits existing state-chartered MHCs to convert their state savings banks to federal charters and *retain their state-chartered mid-tier stock holding company*. This may offer certain charter benefits, particularly those relating to corporate governance under state law (e.g., Delaware, Maryland, etc.), that are not available under a federal mid-tier charter.

Finally, state-chartered savings banks may *retain their state charters and form federal MHCs* chartered and regulated by the OTS. This alternative, which is available in most states, may offer savings banks the best of both worlds because it preserves the benefits of a state charter and establishes the OTS, rather than the Federal Reserve Board, as the MHC's primary federal regulator.

**Pick the Charter That's Best for Your Bank**

Notwithstanding the popularity of the federal MHC charter, several savings banks have elected to retain their state charters and form state-chartered MHCs regulated by the Federal Reserve Board. There may be several good reasons for retaining a state-chartered MHC (and a state-chartered savings bank), and no single charter is best for every savings bank that is considering an MHC. Each institution needs to carefully evaluate the advantages and disadvantages of each charter option before forming an MHC.

**Impact of an Unsettled Market on New Deals**

Going forward, the most significant new challenge for MHCs, as well as for conversion transactions generally, is the unsettled stock market for financial institutions that has existed during the past few months. Changes in market prices of bank and thrift stocks always occur, but volatility in the markets creates pricing challenges for new MHC or conversion offerings because appraisals generally lag the market. As a result, many of the recently completed MHC stock offerings are trading at or below their initial offering prices.

While valuations for MHCs remain near their historic highs, lower valuations are inevitable if thrift and community bank stock prices continue to decline. Lower valuations, however, may be a positive development because they will result in less capital raised and allow for greater stock price appreciation in the future.

**The Appeal of "Private" MHCs**

As we have stated before, even if your savings bank does not have plans to raise capital in the foreseeable future, it makes sense to consider forming a so-called "private" MHC. A private MHC has no public stockholders and, therefore, its mutual ownership is unchanged from that of a "stand-alone" mutual. Forming a private MHC takes about six months and can be done relatively inexpensively. Once formed, however, a private MHC gives mutual savings banks a number of strategic advantages and a host of expansion opportunities, including the ability to raise capital (both common stock and trust preferred stock) without the need for a depositor vote.

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Luse Gorman Pomerenk & Schick, P.C. completed more MHC and conversion transactions than any other law firm in 2004, making us the leading firm nationally for four years in a row. If you have any questions regarding the advantages of the MHC structure, MHC charter alternatives or strategies for raising capital in the current market, please feel free to contact any of the following members of our law firm.

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