

OFFICE OF THRIFT SUPERVISION

Approval of Bylaw Amendments and Application to Modify and Rescind Conditions of Approval

Order No.: 2009-18
Date: March 24, 2009
Docket Nos.: 05848, 18000,
08308, H-3483,
H-4353, H-2265

E*TRADE Bank, Arlington, Virginia (Association), E*TRADE Savings Bank, Arlington, Virginia (Savings Bank), and United Medical Bank, FSB, Baltimore, Maryland (UMB) (collectively, Applicants) have filed, pursuant to 12 C.F.R. § 552.5, applications with the Office of Thrift Supervision (OTS) to amend their bylaws to allow, in certain circumstances, for automatic resignation and removal of directors.

In addition, the Association has requested that OTS modify a condition of approval (Condition 6) imposed by OTS Order No. 2000-02, dated January 10, 2000 (Order) in connection with the Association's acquisition by E*TRADE Group, Inc., Menlo Park, California, (Company). Condition 6 of the Order requires, among other things, that at least one member of the Association's board of directors be an individual who is entirely independent of the Association and its affiliates. The Association has requested that OTS eliminate this requirement.

Also, the Association requests that OTS rescind Condition 17 of the Order, which prohibits the Association and any securities affiliate, as defined in the Order, from sharing common officers unless prior approval is obtained from the OTS Southeast Regional Director.

Background

The Association is a federally chartered, Deposit Insurance Fund (DIF)-insured, stock savings bank, and is a wholly owned subsidiary of ETB Holdings, Inc. (Holdings). The Savings Bank is a federally chartered, DIF-insured, stock savings bank, and is a wholly owned subsidiary of the Association. UMB is a federally chartered, DIF-insured, stock savings bank, and is a wholly owned subsidiary of Holdings. E*TRADE Financial Corporation, a publicly traded savings and loan holding company (Parent), is successor to the Company, and indirectly controls the Association, the Savings Bank and UMB through ETFC Holdings, Inc. and Holdings, its subsidiary savings and loan holding companies.

The Parent is in the process of restructuring the boards of directors of the Association, the Savings Bank, UMB and Holdings, in order to enhance communication

between and coordination among various entities in the Parent's organization, to increase operational efficiencies, and to reduce costs.

The Parent's current board of directors consists of eleven directors, including ten who OTS would consider "independent." The Parent proposes that the Association's board consist of the eleven members of the Parent's board, as well as the Association's President/Chief Operating Officer (CEO), for a total of twelve members. If the Association's board of directors is modified as proposed, the composition of the Association's board of directors would not be consistent with the requirement of Condition 6 that at least one board member be entirely independent of the Association and its affiliates.¹ The Association has requested that OTS modify Condition 6 to eliminate this requirement.

Also, the Association requests that OTS rescind Condition 17 of the Order, which prohibits the Association and any securities affiliate, as defined in the Order, from sharing common officers unless prior approval is obtained from the OTS Southeast Regional Director.

In addition to the revisions to the Association's board of directors described above, the parties contemplate that the Savings Bank's and UMB's boards consist of three officers of the Parent, and the CEO and one other officer of the Savings Bank and UMB, respectively.

The Applicants propose to amend their bylaws to require automatic resignation from the Applicants' boards of: (i) any director of the Applicants who also is a director of the Parent (Parent-Director), who resigns from the Parent's board of directors; (ii) any director of the Applicants who is also an officer of the Parent or an officer of an affiliate of the Applicants (Parent-Officer), who resigns from his or her position as an officer of the Parent or the affiliate; and (iii) any director of the Applicants who is also an officer of such Applicant (Officer-Director), who resigns from his or her position as an officer of such Applicant. In addition, the Applicants propose to amend their bylaws to require automatic removal from the Applicants' boards of: (i) any Parent-Director or Parent-Officer who is removed from his or her position as a director of the Parent or as an officer of the Parent or an affiliate of the Applicants, respectively, consistent with applicable state corporate law, the certificate or articles of incorporation, and the bylaws of the ultimate parent company or affiliate of the Applicants; and (ii) any Officer-Director who is removed from his or her position as an officer of the relevant Applicant, in accordance with such Applicant's bylaws.

¹ The composition of the Association's board of directors would be consistent with the other requirements of Condition 6. These requirements are that at least 40 percent of the Association's board of directors be individuals who are not officers or employees of the Company or affiliates thereof and at least 50 percent of the Association's audit and investment committees be directors who are not officers or employees of the Association, the Company or any affiliates.

Bylaw Amendments

The Applicants' proposed bylaw amendments are not preapproved because they are inconsistent with OTS's regulations for federal stock savings associations set forth at 12 C.F.R. Part 552. Section 552.6-1(f) of OTS's regulations provides that a director may be removed only for cause by a vote of the holders of a majority of the shares then entitled to vote. The proposed bylaws, in essence, contemplate removal of a director if that director: (i) is also a director of the Parent, who resigns from such position; (ii) is also an officer of the institution, the Parent or an affiliate of the Applicants, who resigns from such position; (iii) is also a director of the Parent, who is removed from his or her position as a director of the Parent; or (iv) is also an officer of the institution, the Parent or an affiliate of the Applicants, who is removed from his or her officer position.²

While the proposed bylaws are inconsistent with 12 C.F.R. §§ 552.6-1 and 552.6-2, 12 C.F.R. § 552.5 contemplates that OTS may approve such bylaws upon application. The regulation, however, does not provide any standards for consideration of the approval. Therefore, OTS may exercise its discretion in reviewing any such proposal.

With respect to the provisions described above requiring automatic resignation of a director of one of the Applicants, OTS has determined that it is appropriate for the Applicants to have boards of directors that overlap as proposed, based on the circumstances pertaining to the particularities of the E*TRADE organization. The structure furthers Parent's and Holdings' direct accountability for oversight of the subsidiary savings associations.

The proposed bylaw amendments relating to automatic resignations will facilitate the restructuring of the Applicants' boards of directors and enhance oversight of, communication between and coordination among the various entities, increase operational efficiencies and reduce costs. These proposed bylaw amendments help ensure that the overlapping structure that OTS believes is appropriate remains in place. Without the proposed bylaw amendments, a director could resign from one position, and remain on the board of the relevant institution, thereby reducing the desired overlap. The respective entity could preserve most of the overlap by naming a new person to fill the vacancy and the respective institution could then expand its board, but this entails additional expense and, if there are multiple resignations, this could result in changing the fundamental structure of the board.

With respect to the provision requiring automatic removal if a director of one of the Applicants is removed from one of the positions described above, we conclude that the proposed bylaw furthers the safety and soundness of the respective institution. If

² The standard for removal of an officer of a federal savings association is less stringent than the standard for removal of a director. In this regard, 12 C.F.R. § 552.6-2(b) provides that an officer may be removed by the board of directors when in its judgment the best interests of the association will be served.

such individual is removed, the individual may be hostile toward the institution. If the individual is permitted to remain in the director position, the person may have the motivation and opportunity to take actions that could harm the institution, based on access to confidential information or through other means.

Based on the foregoing, OTS concludes that the adoption of the proposed bylaw amendments is appropriate. Accordingly, the Applicants' applications to amend their bylaws are hereby approved.

Modification and Rescission of Conditions of Approval

OTS has the legal authority to impose conditions of approval on applications, in order to ensure that the relevant approval criteria are satisfied.³ OTS may modify or rescind conditions of approval, provided it has a rational basis for doing so.

OTS imposed Condition 6 to help ensure the independence of the Association's board of directors and audit and investment committees in light of proposed affiliate transactions. OTS concluded that Condition 6 helped ensure that the future prospects and probability of success of the Association were consistent with approval of the acquisition by the Company.

Based on the relevant circumstances, OTS believes that the modification of Condition 6 is appropriate. The Association's board will consist of the Parent's eleven directors (ten of whom are considered independent under Condition 6) and the Association's CEO. This structure will assist the Association's directors in understanding how the Association's operations fit into the entire operations and strategies of the Parent. A completely independent director who did not participate in the Parent's board meetings would not have this perspective. While the Association's chief executive would sit on the Association's board and not the Parent's, that person is a full time employee and should be aware of the Parent's operations and strategies outside of board meetings. Also, significant brokerage operations that were separate from the Association when the condition was imposed have been, or will be, conducted in subsidiaries of the Association. Therefore, the risk that decisions will be made to benefit the Parent and other affiliates of the Association that might not be as beneficial for the Association has been reduced or will be substantially reduced in the near future.

With respect to Condition 17, OTS imposed Condition 17 to protect the Association from risks posed by its holding company's securities activities. OTS concluded that Condition 17 helped ensure that the future prospects and probability of success of the Association were consistent with approval of the acquisition by the Company.

³ See Kaneb Services, Inc. v. Federal Savings and Loan Insurance Corporation, 650 F.2d 78, 83 (5th Cir. 1981).

Given that a significant portion of the Parent's securities operations have already been, or will be, conducted in operating subsidiaries of the Association, the Association will be exposed to the risks inherent in some aspects of the securities activities notwithstanding the condition. The rescission of Condition 17 will allow the Association to share officers with the entities that conduct such operations, without OTS approval, and will help enable the Association to more efficiently integrate the activities of these entities with the Association's activities.

Based on the foregoing, OTS concludes that there is good cause to modify Condition 6 and to rescind Condition 17, as requested in the application. Accordingly, OTS hereby modifies Condition 6 and rescinds Condition 17 of the Order. The remaining conditions of the Order remain in effect.

By order of the Acting Director of the Office of Thrift Supervision, or his designee, effective March 24, 2009.



Grovetta N. Gardineer
Managing Director,
Corporate & International Activities