

OFFICE OF THRIFT SUPERVISION

Approval of Application to Convert to a Federal Stock Savings Association, Holding Company Application, Transfer Application and Trust Powers Application

Order No.: 2007-59

Date: November 9, 2007

Docket Nos.: 18077, H-4451

The Schwab Bank, N.A., Reno, Nevada (Institution), has applied to the Office of Thrift Supervision (OTS), pursuant to 12 C.F.R. § 552.2-6, to convert from a national bank to a federal savings association and has applied under 12 C.F.R. § 563.22(c) to acquire The Charles Schwab Trust Company, San Francisco, California (Trust Company) in a merger transaction. The Institution has also applied to exercise fiduciary powers, pursuant to 12 C.F.R. Part 550. In addition, The Charles Schwab Corporation, San Francisco, California (Holding Company) and related parties,¹ have applied to OTS, pursuant to 12 U.S.C. § 1467a(e) and 12 C.F.R. § 574.3, to acquire the Institution.

The Proposed Transaction

The Institution proposes to convert directly from a national bank to a federal savings association. Shortly after the conversion, the Trust Company, a wholly owned, state-chartered trust company subsidiary of the Holding Company, will be merged into the Institution, with the Institution as the surviving entity. The Institution will continue its current activities, as well as certain fiduciary activities, and will be renamed Charles Schwab Bank. As a result of the transaction, the Holding Company will become a savings and loan holding company.

Public Comments

OTS received thirty-eight public comments addressing the applications. Comments that objected to the proposed transactions (Adverse Comments) asserted that the Institution's Community Reinvestment Act (CRA) assessment area is too narrow, the

¹ The Holding Company's principal owners are Charles R. Schwab and his wife, Helen O. Schwab, who directly or indirectly own or control approximately 17.72 percent of the Holding Company's outstanding common stock. They hold their interests in the Holding Company both in their individual capacities and through certain personal and family-related entities and trusts. The related entities are the Charles & Helen Schwab Living Trust, 188 Partners, LP, and its general partner, Helen O'Neill Schwab Trust, HOS Family Partners, LLC and The Charles and Helen Schwab Foundation. In addition, members of Mr. and Mrs. Schwab's immediate family hold a *de minimis* amount of the Holding Company's common stock (significantly less than one percent), individually or through trusts primarily for the benefit of the Schwabs' children or grandchildren. The companies listed in this footnote are referred to herein as the Related Companies.

Institution should enter into a CRA agreement with California community organizations, the Institution's home mortgage lending to low-to-moderate income communities and its small business lending and loans to small nonprofit organizations are insufficient, the Institution's CRA performance is inadequate, and the Institution should develop a supplier diversity strategy.

Conversion of the Institution to a Federal Savings Association

Section 552.2-6 of OTS's 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 (FDIC); 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 with the requirements of section 5(c) of the Home Owners' Loan Act (HOLA).

The proposed conversion of the Institution conforms to the requirements of section 552.2-6. The Institution is a national bank and is a member of the Federal Home Loan Bank of San Francisco, and its deposits are FDIC-insured. Section 552.13(b)(4) defines "depository institution" to include a national bank. The proposed conversion of the Institution to a federal savings association is permissible under OCC regulations.² The Institution is in compliance with the requirements of section 5(c) of the HOLA.

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's judgment, a necessity for such savings association exists in the community to be served; (iii) if there is 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.³ OTS regulations implementing the HOLA 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.⁴

In addition, OTS 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.⁵ OTS takes this description into account when considering the application and may deny the application or condition approval on CRA grounds.

² 12 C.F.R. § 5.24(f) (2007).

³ Section 5(e) of the HOLA, 12 U.S.C. § 1464(e).

⁴ 12 C.F.R. § 552.2-1(b)(1) (2007).

⁵ 12 C.F.R. § 563e.29(b) (2007).

With respect to character and responsibility, OTS has considered the background and supervisory history of the Holding Company, the Institution and the Trust Company, and the competence, experience and integrity of their management. In considering the supervisory history of the Holding Company, the Institution and the Trust Company, OTS has considered the views of the regulators that have overseen the Holding Company, the Institution and the Trust Company. Based on the above, OTS concludes that this approval criterion is satisfied.

As for the necessity for the Institution in the community, and undue injury to properly conducted existing local thrift and home financing institutions, the Institution will continue its current business activities. Because the Institution has been operating successfully, OTS concludes that there is a necessity in the community for the Institution. Moreover, the change in the charter to a federal savings association will not result in undue injury to existing institutions.

As for the Institution's probability of usefulness and success, based on the Institution's business plan, historical data regarding the Institution, the Institution's proposed capital levels, and competence of management, OTS concludes that there is a reasonable probability of the Institution's usefulness and success. OTS is imposing condition 5 to help ensure that the Institution operates pursuant to an OTS-approved business plan and that changes to and from such a business plan are not detrimental to the Institution. Further, to help ensure the independence of the Institution's board of directors and its audit committee, in light of proposed relations with affiliates, OTS is imposing condition 6 addressing the composition of the Institution's board and its audit committee.

With respect to the provision of credit for housing, the Institution intends to continue offering mortgage products nationwide, will satisfy the qualified thrift lender test throughout the three-year period of the submitted business plan, and has competent management. OTS concludes that the Institution's role in providing credit for housing consistent with safe and sound operations of a federal association is consistent with approval.

The Institution intends to adopt a charter and bylaws that are consistent with the model charter and bylaws for a federal stock institution. Accordingly, OTS does not object to the proposed conversion based on the Institution's charter and bylaws.

OTS reviewed the Institution's plan for compliance with the CRA and the results of the Institution's most recent compliance examination. The Institution recently received a "Satisfactory" CRA rating. The Institution currently provides annual reports to the OCC regarding CRA qualifying loans, investments and services provided outside of the Institution's assessment area.⁶ The Institution has provided a commitment to OTS

⁶ See OCC Conditional Approval #577 dated February 2003.

to provide similar annual reports to OTS to monitor CRA related activities beyond the Institution's assessment area. Although the Adverse Comments objected to the merger application on CRA grounds, as discussed below, we conclude that the matters raised in the Adverse Comments do not provide a basis for concluding that the transaction is inconsistent with the CRA. Accordingly, we conclude that approval of the application is consistent with the CRA.

Holding Company Application

In the proposed transaction, the Holding Company will acquire control of a savings association, as control is defined in 12 C.F.R. Part 574 (Control Regulations). Accordingly, the transaction requires OTS approval under Section 10(e) of the HOLA and under the Control Regulations.

Section 10(e)(1)(B) of the HOLA and the Control Regulations provide that OTS must approve a holding company application seeking permission to acquire one savings association by a company other than a savings and loan holding company unless 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 to the insurance risk of the Deposit Insurance Fund. Also, OTS must consider the impact of any acquisition on competition.⁷ Further, 12 C.F.R. § 563e.29(a) requires that OTS take into account assessments under the CRA when approving savings and loan holding company acquisitions.

With respect to the managerial resources of the Institution, the current senior executive officers of the Institution will continue to manage the Institution. As noted above, OTS has considered the background and supervisory history of the Holding Company, the Institution and the Trust Company, and the competence, experience and integrity of their management. OTS has also considered the backgrounds of the Related Companies. On the basis of OTS's review, OTS concludes that the managerial resources of the Holding Company, the Related Companies, and the Institution are consistent with approval.

With regard to financial resources and future prospects, OTS has reviewed the past operations and financial strength of the Holding Company and concluded that the Holding Company has experienced stable performance, has a high probability of future success, and will be a source of strength to the Institution. The Institution is well capitalized and is projected to remain well capitalized. The Related Companies' financial resources are adequate for their purposes. Based on the foregoing, OTS concludes that the financial resources and future prospects of the Holding Company, the Related Companies, and the Institution are consistent with approval of the holding company application.

⁷ 12 U.S.C. § 1467a(e)(2) and 12 C.F.R. § 574.7(c)(2) (2007).

The transaction will not result in any currently operating, unaffiliated depository institutions becoming affiliated. Accordingly, OTS finds no basis for objection to the transaction on anti-competitive grounds.

With respect to the Holding Company's performance under the CRA, the Institution most recently received a "Satisfactory" CRA rating. Although the Adverse Comments requested that the Institution revise its CRA activities, as discussed below, none of the Adverse Comments provided information indicating that the Institution's CRA performance has been less than satisfactory. Accordingly, the previous CRA performance of the Institution is consistent with approval. Therefore, OTS concludes that approval of the holding company application is consistent with the CRA.

Transfer of Assets Application

The Institution has applied to acquire the Trust Company, a state-chartered trust company that does not have FDIC insurance of accounts, in a merger transaction. Section 563.22(c) of OTS's regulations prohibit such an acquisition without OTS approval. Section 562.22(d) of OTS's regulations provides that in considering such an application OTS will consider: (i) the capital levels of the resulting association; (ii) the financial and managerial resources of the constituent institutions; (iii) their future prospects; (iv) the convenience and needs of the communities to be served; (v) the conformity of the transaction to applicable laws, regulations and OTS policies; and (vi) whether the transaction is fair and equitable and fully disclosed.

As discussed above, the Institution will be the resulting institution, it will meet all capital requirements after the transaction is consummated and it will retain the Trust Company's existing management. Accordingly, capital, and financial and managerial resources considerations are consistent with approval. Further, based on the above, OTS concludes that the future prospects of the Institution are consistent with approval. The Institution will continue the activities of the Trust Company. Therefore, convenience and needs considerations are consistent with approval.

With respect to conformity with applicable law, applicants have informed us that the transaction requires the approval of the FDIC and that they will obtain the necessary approval before the transaction is consummated. In addition, the applicants represent that the merger is consistent with applicable California law. Provided the necessary approvals are obtained, it appears that the transaction will comply with applicable laws, regulations and regulatory policies. The approval of the transaction will be conditioned on the Institution, the Holding Company and the Trust Company obtaining the necessary approvals.

With respect to the fairness of the transaction, the transaction is consistent with approval, because the transaction is an internal reorganization involving only entities

controlled by the Holding Company.

Based on the foregoing, OTS concludes that the transfer application meets all of the requirements of 12 C.F.R. § 563.22(d).

In connection with the merger of the Trust Company into the Institution, the Holding Company filed a notice with OTS in order to claim the exemption from the quantitative limits of Section 23A of the Federal Reserve Act, and 12 C.F.R. §§ 223.11 and 223.12, and the collateral limitations of Section 23A and 12 C.F.R. § 223.14, pursuant to the internal corporate reorganization exemption set forth at 12 C.F.R. § 223.41(d) (Exemption). OTS has reviewed the notice, and has concluded that the proposed merger is eligible for the Exemption.

Analysis of the Adverse Comments

The Adverse Comments assert that: (i) the Institution's CRA assessment area is too narrow; (ii) the Institution should enter into a CRA agreement with California community organizations; (iii) the Institution's home mortgage lending to low-to-moderate income communities is insufficient, and the Institution does not engage in small business lending or lending to small nonprofit organizations; (iv) the Institution's CRA performance is inadequate; and (v) the Institution should develop a supplier diversity strategy.

OTS has carefully reviewed the Adverse Comments. With regard to the Institution's CRA assessment area, the Institution's CRA assessment area is consistent with OTS's CRA regulations. With regard to CRA agreements with California community organizations, there is no statutory or regulatory requirement that the Institution enter into such agreements. With regard to home mortgage lending to low- and moderate income communities, OTS has reviewed the Institution's lending and has concluded that it is acceptable. In this regard, the OCC previously concluded that the Institution's "overall distribution of home mortgage loans reflects excellent penetration among borrowers of different income levels, particularly those defined as low- and moderate-income."

With regard to lending to small businesses and small nonprofit organizations, there is no statutory or regulatory requirement that the Institution engage in such lending. With regard to the Institution's CRA performance, certain of the Adverse Commenters asserted that the Institution's CRA rating, which was "Satisfactory", was lower than that of certain other institutions. OTS notes that the Institution has a "Satisfactory" CRA rating, which is indicative of acceptable CRA-related activities. Finally, with respect to supplier diversity, there are no federal regulations requiring supplier diversity.

Based on OTS's analysis of the issues raised in the Adverse Comments, OTS concludes that the Adverse Comments do not provide a basis to deny the applications or to impose non-standard conditions of approval.

Trust Powers Application

The Institution has filed an application to exercise trust powers. In reviewing a trust powers application, OTS must consider: (i) the financial condition of the applicant; (ii) the capital of the applicant and whether it is sufficient under the circumstances; (iii) the applicant's overall performance; (iv) the fiduciary powers proposed to be exercised; (v) the proposed supervision of the fiduciary powers; (vi) the availability of legal counsel; (vii) the needs of the community to be served; and (viii) any other factors OTS considers proper.⁸

With respect to the first three criteria, the Institution is and will be well capitalized, and the current operations of the Institution and Trust Company are profitable. The Institution has represented that it will be well capitalized, with capital exceeding state law requirements. Therefore, OTS concludes that the first three criteria have been satisfied.

As for the fourth criterion, the Trust Company has conducted its trust activities under applicable state laws and regulations, and subject to the supervision of the State of California. The Institution will conduct the same activities as the Trust Company, as well as additional activities that are permissible under state law for California-chartered trust companies. Therefore, OTS concludes that the proposed trust activities are permissible under state laws and regulations and are permissible trust activities for the Institution after the proposed charter conversion. As for the Institution's supervision of the fiduciary powers, the Trust Company received acceptable ratings at its last examination, and the Institution will be continuing the existing business of the Trust Company using the same management, who possess sufficient experience in the proposed fiduciary activities to be conducted. With respect to the availability of legal counsel, the Institution has access to adequate trust counsel. With respect to the needs of the community to be served, the Institution will continue to offer the trust services it currently offers. Accordingly, OTS concludes there is an adequate basis to approve the trust powers application.

Conclusion

Based on the information provided with the applications, OTS's analysis of such information, the representations and commitments provided by the Holding Company and the Institution, OTS concludes that the applications satisfy the applicable approval standards, provided that the following conditions are complied with in a manner

⁸ See 12 C.F.R. § 550.100 (2007).

satisfactory to the West Regional Director or his designee (Regional Director). Accordingly, the applications are hereby approved, subject to the following conditions:

1. The Holding Company, the Institution and the Trust Company must receive all required regulatory approvals prior to consummation of the proposed transaction, with copies of all such approvals provided to the Regional Director;
2. The proposed transaction must be consummated within 120 calendar days from the date of this Order;
3. The Holding Company and the Institution must, within 5 calendar days after the effective date of the proposed transaction: (a) advise the Regional Director in writing of the effective date of the proposed transaction; and (b) advise the Regional Director in writing that the transaction was consummated in accordance with all applicable laws and regulations, the applications, and this Order;
4. On the business day prior to the date of consummation of the proposed transaction, the chief financial officers of the Holding Company, the Trust Company and the Institution must certify in writing to the Regional Director that no material adverse changes have occurred with respect to the financial condition or operation of the Holding Company, the Trust Company, and the Institution, respectively, as disclosed in the applications. If additional information having a material adverse bearing on any feature of the applications is brought to the attention of the Holding Company, the Institution, the Trust 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. The Institution must operate within the parameters of its three-year business plan, and must submit any proposed major deviations or material changes from the plan for the prior, written non-objection of the Regional Director. The request for change must be submitted a minimum of 60 calendar days before the desired implementation date; and
6. At least 40 percent of the Institution's board of directors must be individuals who are not officers or employees of the Holding Company or affiliates thereof, and who have not otherwise been determined by the Regional Director to lack sufficient independence. At least one member of the Institution's board of directors must be an individual who is not an officer, director or employee of the Holding Company or any affiliate, and who is not an officer or employee of the Institution, and who has not otherwise been determined by the Regional Director to lack sufficient independence. At least 50 percent of any audit committee established by the Institution must be directors who are not officers or employees

of the Institution, the Holding Company or any affiliates, and who have not otherwise been determined by the Regional Director to lack sufficient independence.

The Regional Director may, for good cause, extend any time period set forth herein for up to 120 calendar days.

By order of the Director of the Office of Thrift Supervision, or his designee, effective November 9, 2007.

A handwritten signature in black ink, appearing to read "Lori J. Quigley", written over a horizontal line.

Lori J. Quigley
Managing Director
Examinations and Supervision-Operations