SAVINGS AND LOAN ASSOCIATIONS: Three questions regarding rights of supervisor.

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Honorable F. M. Horton, Supervisor
Division of Savings and Loan Supervision
Jefferson City, Missouri

Dear Sir:

We have your letter of recent date which reads as follows:

> "We have a situation in the "A" building and loan association of the Directors acknowledging that, for some time prior to December 31, 1945, they had contemplated liquidation of the association. In February 1946 several of the Directors called at my office with a proposal to liquidate as of December 31, 1945, provided my approval was given with the expressed stipulation that borrowing members could not participate in distribution of the Reserves.
>
> "Under the plan of operation when the shares in question were issued, each member was required to assume the same liability as a shareholder, whether the shares were pledged with a loan or not; and was privileged to participate in the profits on exactly the same basis as other installment shares. That all shares, both pledged and free, were treated as one and the same class of shares (prior to inception of the plan to liquidate) is shown by the records of maturities of these shares down to the present time. Without exception, in requesting departmental approval to retire maturing series, all shares in the series have been matured on the same basis, and never was the point raised that certain shares should be given preference over others.

"It was my position that it would be unfair to permit liquidation of a mutual savings and loan association under a plan providing that of two share accounts issued at the same time, (both assuming the same share liabilities and both having shared equally in the profits) one should participate in the extra profits incident to liquidation and the other should be denied that privilege.

"The members of the Board were quite outspoken in their insistence that liquidation be on that basis, and no other. They made it clear they intended to liquidate the association on their own terms, and would bide their time until they could work it out to their satisfaction. Their position being that they held and/or controlled a majority of the outstanding shares so that no action could be taken of which they did not approve, regardless of how much their position might react to the disadvantage of other members.

"Discrimination between shareholders in liquidation of a savings and loan association had never previously been proposed in any case coming to my attention, it having always been accepted that like shares should receive like treatment. Among the more recent liquidations of associations, operating as has the instant building and loan association, in which no discrimination was made or suggested are: Mexico Building and Loan Association, Steele Building and Loan Association, Dexter Building and Loan Association, Nickel Savings, Investment and Building Association of St. Louis, Mount Olive Building and Loan Association of St. Louis, Sikeston Building and Loan Association, Bethany Savings and Loan Association and Bolivar Building and Loan Association.

"Because of the fact the life of the building and loan association was continued through the year 1946 for the expressed purpose of eliminating certain members from participating in liquidation of their association, and that it is being continued at the present time for no other reason, it would appear it no longer serves the purposes for which it was organized and chartered by the

State of Missouri, and that steps should be taken to wind up the affairs of the association at the earliest possible date consistent with protecting the interests of all members.

"Pertinent facts and observations pertaining to the case, other than set out herein, are contained in the Examiner's Report of March 13, 1947, and a copy of this report is attached for your information.

"In view of the facts as contained herein and in the Examiner's Report, will you please advise as to the following:

(1) As Supervisor of the Division of Savings and Loan Supervision do I have the power to insist that the association be liquidated?

(2) Do I have the power to insist that in fairness to all members, liquidation be as of December 31, 1945?

(3) Do I have the power to insist that all shareholders share equally (in proportion to their interest in the association) in the liquidation?

"I am particularly interested in your opinion on these questions as there appears to be a definite trend towards liquidation of these associations in the smaller towns, and of the smaller associations in the larger cities, due to lack of business in sufficient volumn to permit of profitable operations. Also there is a noticeable tendency on the part of Directors and Officers to treat the winding up of the affairs of their association as the closing-out of their own private enterprise.

"With Reserves greater in proportion to the outstanding share liabilities than ever before and a ready market for good loans at par, or at a premium, the temptation is great to dissolve the corporation and distribute the reserves to the members. At this point is where we now encounter the trend to delay action until 'other' member's accounts have been closed out, or

> greatly reduced. When this condition develops there appears to be no one willing, or in position, to protect the minority shareholders, other than this Department, and our right to take any action has been challenged in no uncertain manner.
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> "Not only will your opinion in this matter affect the instant association, but a parallel case has come to my attention in which it appears probable that minority shareholders have been even more ruthlessly treated, so it is imperative that the Department know the extent of it's powers and how to proceed."

Your letter and the data contained in the Examiner's Report attached thereto show clearly that the holders of a majority of the stock for accounts of the building and loan association by virtue of their position as directors of said association, are manipulating the affairs of the association in such a manner as to gain an advantage for themselves over the other stockholders. Liquidation of the association has been agreed upon and the present acts of the directors are directed towards securing for themselves a preference for their interests over the interests of other shareholders in the distribution in liquidation.

The 1945 Legislature passed a new act governing such associations as the one under discussion. Said act is found in Laws 1945, page 1579. Section 32 of said act reads as follows:

> "The members of an association shall not be responsible for any losses which its capital shall not be sufficient to satisfy, and the accounts of a member shall not be subject to assessment, nor shall a member holding an installment investment account be liable for any unpaid installments thereon. No preference between account holders shall be created with respect to the distribution of assets upon voluntary or involuntary liquidation, dissolution and winding up of an association."

Section 82 of said act provides for the voluntary liquidation of such an association. Said Section 82 reads as follows:

"Any association may, by a majority of two-thirds of the votes cast either in person or by proxy at a special meeting of the members, vote to liquidate, dissolve and terminate its existence. If such a resolution be so adopted, a certificate containing a true copy of such resolution, stating the number of votes cast for and against its adoption, and signed and acknowledged by the chairman of board of directors, president and secretary of such association shall be filed in quadruplicate with the supervisor within ten days after the date of adoption of such resolution. The supervisor, upon receipt of such certificate, shall immediately examine such association. If he finds that such association is in sound condition, he shall make notation to such effect upon one of such quadruplicate certificates and return same to the association, with his approval of dissolution. Upon such approval, the association shall be dissolved and shall cease to transact any new business, but nevertheless shall continue as a corporate entity for the sole purpose of selling, collecting and conserving assets, paying, satisfying and discharging existing liabilities and obligations and making distribution to the members pro rata of the net proceeds of liquidation, and doing all other acts required to adjust, wind up and dissolve its business and affairs. The board of directors shall act as trustees for liquidation. They shall proceed as speedily as may be practicable to wind up the affairs of the association, and, to the extent necessary or expedient to that end, shall exercise all the powers of such dissolved association, and, without prejudice to the generality of such authority, may fill vacancies, elect officers, carry out the contracts, make new contracts, borrow money, mortgage or pledge the property, sell its assets at public or private sale, or compromise claims in favor of or against the association, apply assets to the discharge of liabilities, distribute assets either in cash or in kind among account holders according to their respective rights, after paying, or adequately providing for, the payment of liabilities, and do and perform all acts necessary or expedient to the winding up of

the association. All deeds or other instruments shall be in the name of the association, and shall be executed by the president or a vice president and the secretary or an assistant secretary. The association, during the liquidation of the assets of the association by the board of directors, shall continue to be subject to the supervision of the supervisor, and the board of directors shall report the progress of such liquidation to the supervisor from time to time as he may require. Upon completion of liquidation and distribution, the board of directors shall file with the supervisor a final report and accounting of such liquidation. If the supervisor approves such report and accounting, he shall issue to the Secretary of State in triplicate certification that such association has been liquidated and dissolved, its indebtedness paid, and the net proceeds derived from liquidation distributed to its members. The Secretary of State shall attach to one of such certifications, a certificate that such association has been dissolved and its corporate existence terminated and shall return same, together with copy thereof, to the supervisor, who shall cause such certificate to be filed for record in the office of the Recorder of Deeds in the county or city in which the principal office of such association is located."

It will be noticed that by the foregoing section the members of the association are entitled to their pro rata share of the net proceeds of liquidation. The mere fact that a member had his shares in the association pledged as security for a loan does not, destroy his relationship as a member. Even though his shares are pledged as security for a loan a member is still a member and entitled to his pro rata part of the liquidation.

What the directors in the case you mention are doing is bringing about a situation wherein they and their families and friends will be the principal ones to share in the division of the assets of the association. There is no question but what this procedure violates the spirit of Sections 32 and 82 of the 1945 act, but the question is whether the supervisor of savings and loan associations can do anything about the situation.

Section 5 of the 1945 act reads as follows:

"The supervisor shall have charge of the execution of laws relating to mutual savings fund, savings and loan associations. The supervisor shall have power to institute in the name of the state of Missouri, and to defend actions in the courts of the State of Missouri and of the United States, and shall have such further powers and perform such additional duties as may be provided by law."

By the foregoing section the supervisor is charged with the duty of seeing that the laws relating to savings and loan associations are carried out.

Section 82, supra, of the 1945 act gives the supervisor specific authority to supervise the voluntary liquidation of such an association. It provides as follows:

"The association, during the liquidation of the assets of the association by the board of directors, shall continue to be subject to the supervision of the supervisor, and the board of directors shall report the progress of such liquidation to the supervisor from time to time as he may require. Upon completion of liquidation and distribution, the board of directors shall file with the supervisor a final report and accounting of such liquidation. If the supervisor approves such report and accounting, he shall issue to the Secretary of State in triplicate certification that such association has been liquidated and dissolved, its indebtedness paid, and the net proceeds derived from liquidation distributed to its members. The Secretary of State shall attach to one of such certifications, a certificate that such association has been dissolved and its corporate existence terminated and shall return same, together with copy thereof, to the supervisor, who shall cause such certificate to be filed for record in the office of the Recorder of Deeds in the county or city in which the principal office of such association is located."

Therefore, the supervisor not only has power to supervise the acts of the directors during voluntary liquidation, but he must approve the final distribution of the assets to the members before the liquidation is complete and effective. The acts of the directors in liquidating the association would not be binding if not approved by the supervisor. Consequently, the supervisor is in position to compel the directors to give all members their pro rata share in the net assets of the association even though some of the members have their shares pledged as security for loans. Of course, it would only be those who were members at the time of liquidation who would be entitled to share in the proceeds. If members prior to that time had surrendered their accounts, they would not be entitled to share in the net assets. We do not believe that the law would authorize the supervisor to compel the distribution of the assets as of any other date than the date of liquidation. In other words, he could not compel a distribution of any part of the assets or profits to persons who were not members at the time of such distribution. Our answer to your second and third questions, therefore, is that the supervisor can compel the directors of a savings and loan association in charge of the voluntary liquidation of same to distribute the assets to those who are members at the time of such distribution in proportion to their interest in the association, regardless of whether or not some of the members have pledged their shares as security for loans, but that he cannot compel a distribution to persons who had been members in the past but who are not then members.

Your first question is somewhat more difficult to answer. There is no charge made that the association is insolvent. Neither is there any charge that the association should be re-organized in order to put it on a sound financial basis. Your question is whether or not you can compel a liquidation of the association because of the acts of the directors in manipulating the affairs so as to gain an advantage for themselves over other shareholders.

Section 97 of the 1945 act provides as follows:

"If it shall appear to the supervisor from any report of such association or from any examination made or caused to be made by him,

or from any knowledge or information obtained from any other source, that such association has committed a violation of its charter or is acting unlawfully, or is conducting its business in an unsafe or unauthorized manner, or that its assets are insufficient to justify the continuance of business by such association, or that it is unsafe or inexpedient for any such association to continue to transact business, the supervisor shall give written notice of such facts and circumstances by registered mail to the chairman of the board, president and secretary of such association. The association shall have sixty days within which to correct the matters of which complaint is made in such notice. If such objectional facts and circumstances are not corrected within such period of time, or if an association shall at any time refuse to permit the supervisor to examine its affairs, he may,--or if the board requests the supervisor so to do, he shall,--take charge and possession of such association and its assets."

Subsequent sections of the 1945 act provide what the supervisor shall do after he has taken charge of an association. Section 100 of said Act reads as follows:

"The supervisor upon taking charge of an association shall as soon as practical ascertain the financial condition thereof by an examination of its affairs and, in his discretion, an appraisal of its assets. If it shall appear therefrom that such association is in a condition to safely resume business without reorganization, he shall return the possession, assets and conduct of the business thereof to the directors and officers. If it shall appear that a reorganization will be necessary before such association can safely resume business and that a reorganization is feasible, he shall propose a plan and attempt to reorganize it. If a reorganization plan, when submitted to the members as hereinafter provided, is not approved by the required majority, the supervisor shall liquidate and dissolve such association, and, after payment of all indebtedness, including

> expenses of liquidation and dissolution, shall make distribution to the members of the net proceeds, pro rata to the participation value of their accounts."

If the supervisor should take charge of the association under discussion, he would be required by Section 100, supra, to return the association to the directors and officers because the financial condition is such that it is safe for the association to resume business.

Section 102 of the 1945 act reads as follows:

> "The supervisor, at any time after taking charge of an association, may institute proceedings in a circuit court of the county or city in which such association has its principal office and have himself appointed temporary receiver until it is determined whether such association can safely resume business, or should be reorganized or should be liquidated. If it is determined that the association should be liquidated, the supervisor shall be appointed permanent receiver for liquidation."

We believe Sections 100 and 102 contemplate that an association shall not be liquidated unless its affairs are in such condition that it is not safe for the association to resume business or be reorganized. There is nothing in connection with the actions of the association under discussion which would indicate that persons who deal with the association would lose money by reason of the condition of the association. Legally the association could be required to meet its obligations. The fact that some of the members are misled into surrendering their interests does not affect the solvency of the association. Members who stay in the association will eventually be paid their pro rata part of the assets. If the directors by wrongful representations induce members to surrender their stock, such members could bring an action upon discovery of the fraud on them and secure the benefits they lost by surrendering their stock. We realize that members will not likely resort to legal action to protect their rights, and we realize too that the directors owe a duty to protect all members of the association, which latter duty

they are apparently not performing, but we do not believe the law gives you the right to liquidate an association because of the acts you mentioned in your letter.

Conclusion

It is, therefore, the opinion of this office (1) that the supervisor of savings and loan associations cannot compel the liquidation of an association because the directors are delaying voluntary liquidation in order that minority shareholders will surrender their shares and drop out of the association before liquidation, with the result that the majority members will divide the assets of the corporation; (2) that the supervisor of savings and loan associations cannot compel an association to liquidate as of any certain date in the past; and (3) that the supervisor can compel the directors upon voluntary liquidation of savings and loan associations to pay all members their pro rata part of the assets even though some members have their interests pledged as security for loans.

Yours very truly,

Harry H. Kay
Assistant Attorney General

APPROVED:

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