ILDING AND LOAN
SSOCIATIONS:

To segregate assets of an association it is not necessary to have a temporary receivership; supervisor may dismiss the temporary Receivership proceeding; intervening shareholders would have right to protect their property only when the supervisor is engaged in wrongful acts or is guilty of fraud or collusion. Several method proposed for obtaining voice of shareholders as to management of the associations. Permanent receivership cannot be dismissed by supervisor.

June 3, 1937

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Honorable J. W. McCammon
Supervisor, Bureau of
Building & Loan Supervision
Jefferson City, Missouri

Dear Mr. McCammon:

This is to acknowledge your letter as follows:

> "I will appreciate your answer to the following questions--
>
> "1. Is it a fact that Mr. Catlett is correct, as indicated in the Kansas City newspaper clippings herewith attached, in asserting that there is a Missouri statute which permits building and loan associations to segregate assets for the purpose of obtaining federal insurance and effecting reorganization without going through the formality of temporary receivership?
>
> "2. What would be our next legal procedure in the event the circuit court of Jackson County should act unfavorably on a motion I might file to take certain associations out of temporary receivership?

"3. What would be the legal status of any "group" of intervening shareholders who might have in mind court procedure in opposition to any plan of reorganization I might submit for court approval? Would the ending of such receivership disarm any "group" of intervening shareholders or could they still proceed?

"4. What is the most practicable way, within the law, to obtain expression from a representative body of shareholders as to the choice of a majority in the matter of ousting one management and electing a substitute management? And, what would constitute a representative body of shareholders? Inasmuch as some of the associations have from two to three thousand shareholders widely scattered as to location, it would be a prolonged task to reach every one of them with a letter and await their reply which would probably dribble in with reference to their choice of a board of directors. Moreover, because of distance, it would be impossible almost to organize a mass meeting that would be attended by all of the shareholders. Since an association belongs to its shareholders, it is my thought that such shareholders have a right to do whatever they please with such association in the matter of choosing official personnel, etc. It is the tendency, of course, for certain "groups" in each association to obtain as many proxies as possible and vote

> their own "group" plans into effect. Thus, in final analysis, permitting a "group" minority to dictate a plan which might be objectionable to a majority of shareholders were it possible to get a complete vote of all shareholders within a reasonable length of time.

"There can be no possible doubt that the Kansas City associations herein under discussion should be fumigated and reorganized, but is temporary receivership actually necessary to such reorganization? What I would like to do, if it is legally possible, would be to immediately end all receiverships, but in so doing not surrender to the crippled associations nor make any concessions whatever in the matter of personnel of management where such personnel is not entirely in the clear as to the administrative methods.

"Now I come to another question as follows:

> "Where a temporary receivership has already been made permanent-- as in the case of the Merchants Association, for example-- what could we do, if anything, in the way of dismissing such receivership inasmuch as it is no longer temporary, although the former Supervisor is quoted as promising that the receivership would be only temporary for the purpose of segregation of assets as a preliminary to obtaining insurance?

"After I get your answer to the legality of the foregoing proposition, I will then look further into the administrative practicability of my tentative proposition of dismissing temporary receiverships by way of wiping the slate clean of Mr. McBride's administrative acts and starting over again toward speedy reorganization of distressed associations."

The newspaper clippings appended to your letter quote Mr. Catlett as saying:

> "There is a statute in your (Missouri) state which permits such reorganizations without receiverships. We have felt that it was unwise to go through Court procedure to achieve this result, because it was difficult to live down the stigma of even a temporary receivership."

The statement of Mr. Catlett was made when he addressed an audience of Building and Loan executives. In Kansas City there are several building and loan associations in receivership, some temporary and others permanent. The purpose of said receiverships was primarily to segregate assets in order to obtain insurance of shares with the Federal Insurance Corporation.

We will answer your questions in the order presented.

I.

You inquire if there is a statute in this state which would permit reorganization of building and loan associations, particularly to segregate assets without the necessity of a court proceeding.

There is a statute in Missouri which in our opinion permits of the segregation of assets. Said statute is Section 5593, Laws of Missouri, 1935, p. 201. This statute is quite lengthy, but we are going to quote the pertinent part because it is all inclusive, and for the further reason that we have not found any court decision interpreting said part of said statute. We quote:

"And any building and loan association shall have the power to provide in its by-laws for the creation and establishment from time to time of a 'participating reserve fund', in which may be placed any or all real estate owned by the association and any loans and/or other assets of doubtful value, the same to be selected by the board of directors, the book value of the assets in said reserve fund to be apportioned pro rata in reduction of the book value of the stock of the association then outstanding, subject to the approval of the supervisor of building and loan associations. Such reserve fund shall be and remain a seperate (separate) fund from the other assets of the association to be liquidated and shall be represented by a class of stock to be known as 'participating reserve shares' of the association to be issued to those stockholders of the association pro rata, the book value of whose stock has been reduced by the creation of such reserve fund. In the liquidation of said reserve fund all the proceeds from the sale of said real estate or collection or liquidation of said loans or other assets shall be paid to the holders of said participating reserve shares, at such times as the board of directors shall determine. All losses, if any, that may occur in said reserve fund shall be absorbed by the holders of said participating reserve shares. The association, if so provided by by-law, may transfer and/or convey title to the assets in said reserve fund, or any part thereof, to three trustees selected by the board of directors, who may be officers of the association, under a trust agreement defining the powers and duties of the trustees, who may issue 'participating reserve certificates', instead of participating reserve shares', to said stockholders entitled thereto, as provided above, giving all the rights and subject to all the liabilities herein pro-

vided as to 'participating reserve shares'. And upon the surrender to the association of the outstanding stock in the hands of a member of such association there shall be issued to such member new stock certificates of the association evidencing the reduced value of the stock surrendered, and in addition to such new stock certificates the reserve shares or reserve certificates to which such member is entitled, as above provided. Such reserve shares or reserve certificates issued to a borrowing member who had his stock up as collateral for a loan shall be pledged as additional collateral for such loan, and the borrowing member shall continue to make installment payments on his loan, as provided in the note or bond and deed of trust securing said loan, and upon payment of the loan in full the directors may apply as a credit on the loan the then value of the reserve shares as determined by the board of directors, after taking into consideration any estimated losses sustained in such reserve fund. In making reports and statements to the supervisory department of the state, the value of such a reserve fund undistributed shall be included as a part of the assets of the association and be classified as 'participating reserve fund.' Provided, however, that any building and loan association may in the discretion of the board of directors create more than one such participating reserve fund under the provisions of this act. And any building and loan association may in the sale of its real estate take stock in the association in payment of the purchase price or any part thereof, at such price and upon such terms and conditions as the board of directors by resolution may approve."

Assuming the constitutionality of the above statute, it is our opinion that a building and loan association may segregate its assets without the necessity of going into either temporary or permanent receivership.

While we assume the constitutionality of said statute, we do not wish to be understood as even intimating that it may be unconstitutional for the reason that a building and loan association is a"quasia public financial institution", and the state by an exercise of its police power regulates and controls such association. State ex rel. vs. Farm & Home Savings & Loan Assn. of Missouri, 90 S. W. (2d) 93.

II.

The legal procedure to be taken in the event the Circuit Court of Jackson County acts unfavorably on a motion you might file to take associations out of temporary receiverships, does not bother us. What is perplexing to us is whether or not the Circuit Court has any discretion other than to grant a motion filed by you to dismiss a temporary receivership. If the Circuit Court has no discretion,but must enter an order of dismissal at your request, then, of course, a writ of prohibition would be a legal procedure in order to protect your rights; or a writ of mandamus could be employed to compel the court to enter an order of dismissal.

Directing our attention to the premise of your right to have a motion to dismiss sustained by the Circuit Court, we find that by virtue of Section 998 R. S. Mo. 1929, the Court,or Judge thereof in vacation, has power to appoint receivers; also by virtue of Section 5627, Laws of Missouri, 1931, pp. 163, 164, the court must appoint the Supervisor temporary receiver if action is instituted in the Circuit Court by the Supervisor. Therefore it is the court

that appoints the Supervisor as receiver, and whether the Supervisor can thereafter control the dismissal of the suit is a close question. Corpus Juris Vol. 53, Article 572, p. 353, has the following to say as to the dismissal of pending litigation:

> "The general rule that the right of a plaintiff to dismiss his action is not an absolute right, but may be denied in the discretion of the court, applies to actions by receivers."

Corpus Juris Vol. 18, Article 11, pp. 1151, 1152, has the following to say:

> "Plaintiffs who act in an official capacity for the public in bringing a suit, as for instance selectmen, overseers of the poor, etc., being the only parties plaintiff before the court, may discontinue such suit, during the continuance of their term of office, where they all concur in such discontinuance."

The only case we have been able to find in Missouri analogous to the present question is State ex rel. vs. Flitcraft, 36 S. W. 675. The above case was a proceeding by mandamus to compel a Judge of the Circuit Court to reinstate a receivership filed by the then ex officio Supervisor of building and loan associations which was dismissed by him without the consent of the attorney-general. The Supervisor, after instituting the receivership with the attorney-general representing him, as provided by statute, dismissed said receivership without the knowledge and consend of the attorney-general and filed another receivership involving the same association in a different Division of the Circuit Court of St. Louis City. The attorney-general filed a motion to reinstate the first receivership, and upon a hearing of said motion the Circuit Court dismissed

same, and then a writ of mandamus was brought in the Supreme Court to compel the reinstatement of the first receivership proceedings. The Court in its opinion succinctly states the position of the various parties litigants:

> "It is insisted by the attorney-general, the relator herein, that as the suit affects the public interests, the state is the real party in interest; that respondent is merely a nominal party, and as, in such proceedings, it is made the relator's duty by the act to represent the state, that respondent had no authority to have the suit stricken from the docket; that the order to that effect was without authority, and that the case should be reinstated on the docket. This position is controverted by the respondent, who contends that the supervisor is not a mere nominal party having no interest or control of suits instituted by him, under said act against building and loan associations, but that it is for him to determine whether any such action shall be begun and when. Ordinarily, a person in whose name a suit is instituted has the right to dismiss it any time before its final submission, and, unless actions brought by the supervisor under said act against building and loan associations be an exception to this general rule, the demurrer to the return must be overruled and the peremptory writ denied."

The Court held that the Supervisor had a right to dismiss, and that his bringing of the action under the statute was not an exception to the general rule that a person instituting a suit had the right to dismiss it. The Court said: (p.678)

> "By the express terms of the act the supervisor is clothed with discretionary power to determine whether the suit shall be to enjoin the association from prosecuting its business temporarily or perpetually, or for injunction and its dissolution, and the settling and winding up of its affairs, or for any and all of said remedies combined, as he may deem necessary; and it seems to logically follow that if, after the institution of such a suit, he should be satisfied that it had been improvidently brought, or for any other cause that it should be dismissed or stricken from the docket, he might have it done, without the knowledge or consent of the attorney-general. To the supervisor belongs the power to investigate the affairs of building and loan associations under said act, and to institute actions against them for the purposes under the circumstances therein named; and, while the attorney general is required to conduct such actions in the name of the state as plaintiff at the relation of said supervisor, the manifest intention of the legislature was to furnish a lawyer of known ability to conduct such suits, but not to confer upon him the power to take charge of and manage the same to the exclusion of the supervisor, but rather subject to the right of the supervisor to have any such actions dismissed or stricken from the docket or disposed of

> as might seem to him to be expedient. We therefore conclude that the suit in question is not an exception to the general rule, and that the supervisor had the right to dismiss it in disregard to the wishes of the relator."

The above case has never been overruled or discussed, but was cited by the St. Louis Court of Appeals in Corbett vs. Lincoln Savings & Loan Association, 223 Mo. App. 329, 339.

In the Corbett case the holding intimates that if the Supervisor (Finance Commissioner) for the purpose of shielding an association from being molested by courts when the association was conducting its affairs wrongfully, that the Supervisor could not preclude a private citizen or shareholder to seek a remedy in the courts to have his wrongs remedied.

In Hackler vs. Farm & Home Savings & Loan Assn., 6 Fed. Sup. 610, the District Judge said the following: (p.615)

> "It is conceivable that upon the disability of the state supervisor or his wrongful unwillingness to proceed, a shareholder might, with appropriate averments, obtain the favorable consideration of a chancellor. Such was the intimation in Corbett v. Lincoln Savings & Loan Association, 223 Mo. App. 329."

However, the District Court in the Hackler case, supra, had the following to say concerning the Supervisor: (p. 616)

> "* * * * The statute contemplates the appointment of the building and loan supervisor as receiver. Such was its entire object.
>
> * * * *

"In view of the foregoing, it must be held that complainants as shareholders or simple contract creditors do not possess the right or have the capacity to ask this court to appoint a receiver."

The Court further held: (p.613)

"Neither can it be contended that the complainants have rights equal to that of the building and loan supervisor in bringing about a receivership. It does not seem reasonable that it was the intention of the Legislature to clothe the building and loan supervisor with no greater authority than that possessed by a shareholder or a creditor.

* * * *

"In the exercise of its police power, the sovereign state of Missouri has undertaken the supervision and regulation of building and loan associations. There has been created the office of building and loan supervisor. Such officer is clothed with express power to inquire, by full and complete examination, into the operation of each of the associations organized within the state and doing business under his supervision. He has authority to correct illegal practices, or, as an alternative, he may take over the management and control of the association. In case of insolvency, and for the purpose of enabling

> him to secure an adjudication upon the rights of all interested parties, he could, acting through the attorney general and in the name of the state of Missouri, procure his own appointment as receiver. This is the remedy provided by the state under its regulatory power for the protection of the rights of all persons whomsoever." (p. 613)

The Supreme Court of Missouri, Division No. 2, in State ex rel. Wagner vs. Farm & Home Savings & Loan Association et al, 90 S. W. (2d) 93, said the following concerning building and loan associations: (p.96)

> "Building and loan associations are quasi public financial institutions, and for the protection of them the state of Missouri has by the act of 1931, provided special inquisitorial, supervisory, and regulating laws which are specific, adequate, complete, and therefore exclusive. State ex rel. Moberly v. Sevier, Judge (Mo. Sup.) 88 S. W. (2d) 154, not yet reported (in State reports). Building and loan associations, like banks, trust companies, insurance companies, and railroads are quasi public corporations as to which the state may exercise its police power and may assert its sovereign rights of regulation and control in the preservation and furtherance of public well-being. Section 5 of article 12, of the Constitution of Missouri; Hackler v. Farm & Home Savings & Loan Association of Missouri (D.C.) 6 F.Supp. 610; Koch v. Missouri-Lincoln Trust Co. (Mo.Sup.) 181 S.W. 44; State ex rel. Missouri State Life Insurance Co. v. Hall, 330 Mo. 1107, 52 S.W. (2d) 174."

See also 78 A. L. R. 1090, 1104, incl.; State ex rel. vs. Hall, 52 S. W. (2d) 174, 177.

From the above it is our opinion that as Section 5627 gives to the Supervisor the right to institute proceedings in the Circuit Court to have himself appointed temporary receiver, and as the Supreme Court of Missouri in State ex rel. vs. Flitcraft, supra, held that the right to dismiss by the Supervisor was not an exception to the general rule, we conclude that the Supervisor absent fraud or collusion or wrongful act on his part, would be entitled to dismiss a temporary receivership in which he was party plaintiff. If a temporary receivership is to be dismissed a motion should be filed by the Supervisor stating the reasons for dismissal, and we are certain that if the reasons are good and sufficient that the Circuit Court will entertain the motion and dismiss the action. If the Circuit Court does not dismiss the temporary receivership upon proper motion and showing, then the Supervisor could apply to a superior court for relief, and if it was shown that a temporary receiver was not needed, we are certain that the Appellate Court would command the lower court to follow the wishes of the Supervisor.

III.

If a receivership is dismissed then intervening shareholders cannot further proceed, in our opinion. As stated in the second point of this opinion, the courts will not entertain petitions of intervening shareholders unless there be fraud or collusion on behalf of the Supervisor so as to deprive a shareholder of his rights. Hackler vs. Farm & Home Savings & Loan Assn, 6 Fed.Sup. 610; Corbett vs. Lincoln Savings & Loan Assn., 223 Mo. App. 329.

IV.

We agree with you that the permitting of a group minority to dictate the management of a reorganized building and loan association should not be tolerated. However, the obtaining of an expression from a representative body of shareholders, or the choice of the majority thereof, is a matter attended with some difficulty. We suggest several plans that could be used:

a. Give notice to the shareholders of the meeting by mail, stating the purpose of the meeting, date, and place, and also notice in a newspaper which would likely be read by a majority of the shareholders. The letter could outline your difficulty and the reason for selecting new management.

b. You could call a representative group of shareholders- say perhaps forty or fifty- and ask them to appoint a shareholders committee for the purpose of selecting a management, and obtaining proxies from shareholders to vote for the management they select.

c. You could select fifteen or more names which would be acceptable to you as the management, and ask each shareholder to indicate his or her choice. At the same time you could request them to signify whether they would be present and vote thusly, or if not present to sign a proxy to the individuals such desire.

The Supervisor is charged with the duty of exacting proper administration of building and loan associations by its officers; Section 5624, Laws of Missouri, 1931, p. 161, specifically requires the Supervisor to make an examination into "the mode of conducting and managing its affairs * * * the action of its directors". And Section 5627 permits the removal of officers and directors upon application of the Supervisor. Thus it is your duty to insure proper management of building and loan associations. However, as the association belongs to the shareholders their wishes in the matter should be the determining factor, providing they are apprised of all the facts concerning the actions, past history and character of the management. In other words, as far as the shareholders may know an officer of an association may be acceptable to them, but if they knew his background their decision would be otherwise.

V.

Section 5627, Laws of Missouri 1931, p. 163, reads in part as follows:

> "The Supervisor may at any time after he takes charge of the assets and affairs of an association, institute proceedings in the Circuit Court in the city or county in which said association has its principal office, and have himself appointed temporary receiver until it is determined whether or not such association can resume business; or appointed receiver for the purpose of winding up its affairs.
>
> * * * * *".

Thus, when you are appointed permanent receiver it would be for the purpose, we assume, of winding up and liquidating the association. Therefore it is our opinion that you would not have the right to dismiss a permanent receivership. Of course you can reorganize the association or sell all of its assets to another association.

If it was represented to the associations that the receiverships would be only temporary and solely for the purpose of segregation of the assets as preliminary to obtaining insurance, we believe your motion, if you decide to dismiss the temporary receiverships, should so state that fact, coupled with the further pleading that the associations can segregate by virtue of statute at less expense and to the best interests of the associations.

Trusting that the above answers your questions, and that if you have further need of elaboration upon that which we have written kindly communicate with us and we shall write further.

Yours very truly,

James L. HornBostel
Assistant Attorney-General

APPROVED:

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JLH/R