

HB

703

STATE
of ALASKA

MEMORANDUM

DEPARTMENT OF COMMERCE & ECONOMIC DEVELOPMENT

TO: Members of the Committee

DATE: December 28, 1977

FILE NO:

TELEPHONE NO:

FROM: Julius J. Brecht, Director *JB*
Division of Banking & SecuritiesSUBJECT: HB 703
Savings Association Act
Amendment Bill Narrative
Supplement

The proposed savings association legislation before you provides a number of changes to the Alaska Savings Association Act (ASAA) AS 06.30. The present law was enacted in 1961 and has undergone little change since that time. A large portion of the provisions of this bill are then of a "housekeeping" nature and are proposed to streamline the administration of ASAA, i.e., to provide clear, unambiguous procedures and guidelines by which state-chartered savings associations will be regulated in this state.

The major provisions of the bill include (1) detailed association chartering procedures; (2) branch office application procedures; (3) establishment of stock savings associations; (4) procedures for conversion from a mutual savings association to a stock association; (5) fixed interest savings accounts; and (6) updating of the loan provisions.

The following is a section-by-section review of the provisions of the bill.

Section 1. (AS 06.30.015). This section adds two new paragraphs to the powers of the commissioner. The proposed powers are to require an association to establish a reserve or charge off an asset classified as a loss in an examination report. In addition, an association would be required to charge off all debts more than 6 months past due unless they are adequately secured and the association is in the process of collection. These provisions are similar to AS 06.05.015(10) and (11) of the Alaska Banking Code and are necessary to ensure the sound condition of an association.

Section 2. (AS 06.30.025). This section repeals reference to inconsistencies with the FSLIC requirements. Obviously the commissioner cannot adopt regulations that would require or allow state-chartered savings associations to engage in activity that would jeopardize their insurance of accounts through FSLIC. That is, these associations must under AS 06.30.365 have such insurance as a pre condition to conducting a savings association business in this state. The deleted language is unnecessary and undermines the authority of the state to regulate state-chartered institutions.

Section 3. (AS 06.30.030). These amendments are proposed to set a policy that the commissioner shall administer the chapter in the best interest of a sound and competitive banking and savings system.

Section 4. (AS 06.30.035). The existing law relating to the incorporation and certification of savings associations is burdensome and difficult to administer. It in effect is a one step process, i.e., once the commissioner approves the petition for incorporation, the association may conduct a savings business. The procedure is as a practical matter more complex. What is needed is a two step process: 1) approval of incorporation by the department which allows the incorporators to organize the association; and 2) issuance of certificate of authority by the department, which allows the association to carry on a savings business. The amendments to AS 06.30.035, 45, and 60 provide a clear, reasonable, and workable procedure for the establishment of a state-chartered savings association in this state. This procedure is similar to that which was adopted by the Oregon Legislature in 1975 (ORS 722.014-028).

Under this section, applicants would submit their articles of incorporation with their application for incorporation of the association. The application would be investigated by the department, and if approved, filed and a certificate of incorporation issued. Under (e) of the section, the applicant would pay all reasonable investigation expenses incurred by the department, thereby relieving the Alaska taxpayer of an unfair burden. If the department does not act within 30 days, the application is considered accepted, and the time period of up to one year for approval or denial of the application by the department begins.

Under this section, the organizers may form a mutual savings association (capital base is the deposits of the association) or a stock association (capital base is the stock of the association sold to the public).

Section 5. (AS 06.30.040). The present law sets out an example of acceptable bylaws for an association. However, the contents are somewhat dated, e.g., reference to savings books, and unnecessary, e.g., requiring the commissioner's approval of amendments. Bylaws are the rules of conduct of business of a board of directors and should be determined by them within certain limits. However, requiring prior approval of the commissioner involves the department too much in the management of the association. The proposed amendment outlines the minimum requirements for bylaws acceptable under the law. It is my view as a matter of legal drafting that detail such as is presently found in Section 40 of the chapter is unnecessary and inappropriate in a statute. The approach proposed in this amendment is more workable for the incorporators and follows that of the 1975 recodification of the Oregon Savings Association Act (ORS 722.022).

Section 6. (AS 06.30.045). This section sets out the procedure for an association to obtain a certificate of authority to conduct a savings association business. The department would issue the certificate if in the case of a stock association the capital and surplus required by the department have been fully paid in cash in the amount required by the department and a list of stockholders is submitted to the department. Similarly, for a mutual association, the initial subscription of the individual subscribers would have to be fully paid in cash in an amount required by the department. In addition, for either type of

association, a copy of the adopted by-laws would have to be filed with the department and insurance of accounts through FSLIC would have to be obtained, and the association would have to have complied with all requirements of the chapter. The procedure is similar to that which was adopted by the Oregon Legislature in 1975 (ORS 722.036).

Section 7. (AS 06.30.060(b)). This section updates the minimum capital requirements for establishing a mutual association. The provisions are similar to that of the Federal Home Loan Bank Board which reviews applications for FSLIC insurance.

Section 8. (AS 06.30.060(e)). This section is amended to provide explicit guidelines for the establishment of an expense fund in the context of a mutual savings association and a stock association. The amount of the expense fund is left to be specified by the department. The expense fund is to be used by the organizers to pay the expenses of organizing the association. The size of the fund reasonably necessary to cover the expenses can be established by regulation.

Section 9. (AS 06.30.060(f)). This section provides that contributions made to the expense fund may be paid back after the additions required by AS 06.30.445 to the surplus and reserve account have been made. Section 445 is being amended under Section 24 of this bill and provides that at the close of each calendar year after the payment of all expenses, an association must before declaring a dividend, transfer to a general reserve or surplus account an amount equal to at least 10% of its net earnings until it equals at least 12% of the savings liability. The change to section 60(f) is proposed to base the payment to the contributors on the association's turning a profit and not on an arbitrary amount as provided in the present law. The 1975 recodification of the Oregon Savings Association Act follows this approach (ORS 722.044(2)).

Section 10. (AS 06.30.060(h)). This section provides the minimum capitalization required to establish a stock association. The requirements are the same as for a mutual association. Minimum savings subscriptions are also required.

Section 11. (AS 06.30.090). This section repeals any reference to a change of location of an association. The procedure for changing a location, or establishing a new branch or agency is set out in AS 06.30.335 (see section 21 of the bill). The section also repeals AS 06.30.090(4) and (5) because they are unnecessary. Paragraph (3) requires the commissioner to issue a certificate of approval. The working relationship between the department and FHLBB need not be reenforced by statute for the reasons stated in Section 2 of this analysis.

Section 12. (AS 06.30.105). This section sets out clear and reasonable guidelines for proxy solicitations in the context of mutual savings associations and stock associations.

Section 13. (AS 06.30.110). This section is amended to make clear that the prohibition against charges specified in the section does not prevent payment being made for the purchase of stock in a stock association.

Section 14. (AS 06.30.115). This section is amended to provide specifically that a stockholder of a stock association has a right to inspect the general books and records of the association except for the loan and savings records of other members.

Section 15. (AS 06.30.140). The maximum number of directors allowed is changed from 15 to 25. Present Alaska corporation law (AS 10.05) and the banking code (AS 06.05) provide for the higher maximum. The higher maximum gives the association more flexibility in establishing a board of directors or adding to it.

Section 16. (AS 06.30.145). (a) of this section amends the minimum required savings account for a director of a mutual savings association to \$1,000. This number is thought to be more realistic in light of the Alaska cost-of-living and cost-of-doing-business. Under (b) of this section, a similar requirement is established for stock associations. Under (c) of the section, each director must take an oath that he will perform the duties of his office and that the oath will be filed with the department each year. A similar provision is found in the Alaska Banking Code (AS 06.05.435).

Section 17. (AS 06.30.270). This section is amended to apply explicitly to mutual savings associations and to stock associations. A stock association must maintain a record of stocks and stock transfers.

Section 18. (AS 06.30.280). This section expands and/or makes specific the powers of an association, e.g., paragraphs 6, 7, 8, 9, 10, 13, 14, 16 and 18 are new.

Paragraph 6 makes clear that an association may declare and pay dividends.

Paragraph 7 allows an association to sell mortgage loans to federal agencies or other savings associations. Under this provision, state-chartered associations would be allowed to package their loans. This process has become the practice in the savings association industry throughout the country in the time since ASAA was enacted. It allows an association subject to heavy loan demand to sell mortgages to another institution whose loan demand is not as heavy. The purchaser-association turns a profit in the transaction through the rate differential (the rate of interest on an older loan may be lower than the rate at the time of the transaction) or a discount on the loan purchased.

Paragraph 8 allows an association to collect and protect their collateral position on a loan. For example, on a second mortgage, the association might take a second deed of trust on a house and/or an assignment of a savings account to secure a loan. This practice is followed in the savings industry.

Paragraph 9 allows an association to offset debts against a member's savings account. This practice is generally followed in the bank and savings association industry.

Paragraph 10 allows an association to obtain insurance on mortgages in the best interest of the borrower. For example, an association may wish to ensure the differential between the regulatory maximum specified in AS 06.30.500 and the amount desired by the borrower, as allowed by that section. In this way, the down payment on a home or mobile home loan may be reduced.

Paragraph 13 is a general statement to make clear that an association may make loans in accordance with the chapter.

Paragraph 14 allows an association to deposit its surplus cash in a bank account thus enabling the association to write checks to customers against their accounts. The paragraph also allows an association to deposit its securities with a correspondent bank for safekeeping. This practice is generally followed in the savings association business.

Paragraph 16 allows an association to act as an escrow agent. It is the practice in Alaska for a bank to act as an escrow agent on loans made through the bank. This provision is particularly useful to savings associations whose primary business is that of providing home loans.

Paragraph 13 allows an association to dissolve and wind up its business. The provision is an obvious necessity when an association wishes to wind up its operation voluntarily.

Sections (4), (9), (10), and (11) of the present law, AS 06.30.280 are not reenacted for several reasons.

Paragraph 4 allows a savings association to take property by gifts, devise, or bequest and is inapplicable and inappropriate to a savings association business.

Paragraph 9 allows an association to insure its accounts in accordance with provisions of the chapter and is unnecessary in that insurance of accounts is mandated by AS 06.30.365.

Paragraph 10 allows an association to qualify as a member of the FHLB and is unnecessary, i.e., an association becomes a member of the FHLB by obtaining insurance of accounts through FSLIC as required by AS 06.30.365.

Paragraph 11 allows an association to become a member of a trade association which promotes savings associations. Membership in a trade association should be a business decision of the board of directors and is, in my view, not a power of the association and is an inappropriate subject of a statute.

Section 19. (AS 06.30.295). The present law prohibits the payment by an association of a fixed rate of interest on accounts. When the Alaska law was enacted in 1961, a fixed rate of interest was not generally allowed on the federal level or in other states. However, in the 17 years since that time, the savings association industry has changed dramatically. Fixed rate of interest and/or fixed term accounts are now allowed for federally-chartered savings associations. These types of accounts must be allowed for state-chartered institutions if they are to compete effectively with their federal counterparts for the Alaskan depositor. This section provides that authority.

Section 20. (AS 06.30.330). The present law in effect provides that federally chartered savings associations may engage in any activity allowed for a state-chartered association. The proper place to provide for powers of federal associations is in the federal law not in the state law. The state law cannot be enforced on behalf of federal institutions and is misplaced in being made a part of the ASAA. The proposal is then to repeal the second sentence in this section referring to federal associations.

Section 21. (AS 06.30.335). This section sets out a clear procedure for the establishment of a branch or agency of an association or for the change of location of the home office, branch, or agency of an association. This section generally follows the applicable proposed application procedures for a new association found in Sections 4 and 6 of this bill. The cost of the investigation incurred by the department would be paid by the association. The rights conferred by a certificate of authority must be exercised by the association within one year from the date of issuance or else the certificate lapses.

Section 22. (AS 06.30.375). Two minor drafting changes are made in this section. The first allows a depositor to open a savings account with the equivalent of cash, e.g., a check, as well as cash. The second change gives the depositor the right to "receive" not "participate" in dividends.

Section 23. (AS 06.30.430). This section requires an association to submit upon request of the department a report of inactive savings accounts. The section also allows for a service charge for reasonable costs incurred in maintaining inactive accounts. Similar provisions are found in the Alaska Banking Code, AS 06.05.

Section 24. (AS 06.30.445). This amendment reorganizes the present statement of section 445 and deletes unnecessary "grandfather" language. The section sets out reasonable reserve and surplus account requirements. Under (c) of the section provision is made to include any federal insurance reserve fund of an association in the general reserve account specified in (a) of the section. The reserve calculations must not include allocations for specific losses (see section 9 of this analysis for further discussion of the reserve requirements). The intent of the section is to provide a strong capital base established in a timely manner.

Section 25. (AS 06.30.455). This section is amended to provide expressly for fixed rate of interest savings accounts in conformance with the proposed amendment to AS 06.30.295 (see section 19 of this bill). The thrust of the amendment is to allow associations to pay dividend as prescribed by FHLBB.

Section 26. (AS 06.30.495). The amendment to section 495 allows an association to make a loan secured by a savings account whether or not the borrower is the owner of the account provided the association obtains a lien or pledge of the savings account as a security for the loan. For example, a father may wish to pledge his savings account against a loan made by the association to the father's son or other family member. Within the narrow limits of lending on savings accounts, this service is provided in a number of states.

Section 27. (AS 06.30.500). This section amends the present restrictive limitations on home loans that have become out-of-date. The proposed language in paragraphs 1-4 and 7 follows a number of provisions of the Alaska Mutual Savings Bank Act at AS 06.15.250. The language was used because of the similarity between savings associations and savings banks and the apparent success of the savings bank law. The limits on investment in mortgages executed to a given mortgagor is set at \$75,000 or 2% of the assets of the association whichever is greater. The limitation for multiple family dwellings is set at \$100,000 or 2% of assets whichever is greater. Paragraphs 5 and 6 are from the present ASAA law. These amendments will allow state-chartered savings associations to compete effectively with other financial institutions.

Section 28. (AS 06.30.505(a)(1)). This section changes the maximum lending limitation from \$45,000 to \$75,000 to conform to the changes made to AS 06.30.500 (see section 27 of this analysis).

Section 29. (AS 06.30.505(c) and (d)). This section provides for loans on mobile homes within certain limitations which are similar to regulations of the FHLB which apply to federal and state-chartered associations.

Section 30. (AS 06.30.555). This section provides that an association may make or acquire a loan by a second lien on improved real estate under certain conditions. Similar provisions are contained in the Oregon Savings Association Act recodified in 1975 (ORS 722.322(3)).

Section 31. (AS 06.30.615). This section is amended to make clear that a stock association may invest an amount less than the sum of its capital stock and surplus as well as its undivided profits and reserve accounts in real estate including buildings and appurtenances as is reasonable for the transaction of its business. The present law is written in terms applying only to mutual savings associations.

Section 32. (AS 06.30.615(b)(7)). This section provides that an association may invest in stock of a wholly-owned subsidiary corporation which has as its purpose the ownership and management of the association's real property. Similar provisions are extended to banks under the Alaska Banking Code, AS 06.05.

Section 33. (AS 06.30.616). This section is new and provides that an association may invest in the capital stock of a service corporation, e.g., a computer processing center, organized under the corporation laws of Alaska under limited conditions. Furthermore, an association may invest in a service corporation whose activities consist of purchasing and disposing of loans and making certain investments authorized by state and federal law. Under (b) of the

section a further restriction is placed on the amount that an association may invest in service corporations, i.e., not more than 5% of its total assets. Similar provisions are contained in the Oregon Savings Association Act recodified in 1975 (ORS 722.004(25) and 308).

Section 34. (AS 06.30.625). This section sets a deadline for the submission of annual reports by the association to the department. The section also requires that the report must be signed by at least three directors in addition to the president and treasurer. This provision will ensure responsible participation by the directors and follows similar language found in the Alaska Banking Code.

Section 35. (AS 06.30.760). This amendment makes clear that section 760 applies to a mutual association converting to a federal association.

Section 36. (AS 06.30.775(a)). This amendment makes clear that section 775(a) applies to a federal association converting to a state-mutual association.

Section 37. (AS 06.30.776). This section is new and applies to the conversion of a state-chartered mutual association to a state-chartered stock association.

Section 38. (AS 06.30.836). This section is new and gives the department authority to dissolve an association formed for the purposes of doing a savings association business but which for some reason has not received its certificate of authority and which the department determines should not open for business. A similar provision is proposed for the Alaska Banking Code (Sec. 06.05.466 of SB 98).

Section 39. (AS 06.30.910(1)). This section is amended to make clear that the chapter applies to mutual and stock associations.

Section 40. (AS 06.30.910(3)). This section makes clear that the commissioner or his designee shall administer ASAA. A similar provision may be found in the Alaska Securities Act at AS 45.55.130(1).

Section 41. (AS 06.30.910(5)). This section makes clear that the term "dividend" may be applied in the context of a return on a savings account or a return on shares of stock. The term is used throughout the chapter and is defined by the context in which it is used in each case.

Section 42. (AS 06.30.910(11)). This section redefines the term "improved real property" in more succinct terms. It is based on the present definition in ASAA and uses language from the FHLB regulations (12 CFR 545.6-14(h)) and is similar to language found in the Alaska Banking Code (AS 06.05.207(f)).

Section 43. (AS 06.30.910(13)). This section redefines the term "member" to include a stockholder in a stock association. The definition is similar to that found in the regulations of FHLB (12 CFR 555.9).

Section 44. (AS 06.30.910(20)). The term "department" is defined.

Section 45. Several sections of chapter 30 are repealed.

- (1) AS 06.30.050 sets out a filing procedure to be followed by the commissioner in processing petitions for incorporation. This section is replaced by the provisions of Sec. 06.30.035 (see section 4 of the bill).
- (2) AS 06.30.055 establishes the period of corporate existence for an association. This section is replaced by the provisions of Sec. 06.30.035(1) (see section 4 of the bill).
- (3) AS 06.30.340 deals with the handling of applications for branch offices. The section is replaced by the provisions of Sec. 05.30.335.(see section 21 of the bill).
- (4) AS 06.30.345 deals with the handling of change of location applications. The section is replaced by the provisions of Sec. 06.30.335. (see section 21 of the bill).
- (5) AS 06.30.350 deals with the revocation of a branch office approval. The section is replaced by the provisions of Sec. 06.30.335. (see section 21 of the bill).
- (6) AS 06.30.435 and 490 provide for bonus plans, which were discarded by the industry sometime ago. The FHLB no longer provides for them in regulating federal savings associations.
- (7) AS 06.30.830 states the obvious in reverse order, i.e., it says that state savings associations and their members must pay the same taxes as federal associations and their members. The provision has no place in state law. The taxation levied on state institutions will be set by state taxation law and is in no way dependent on how a federal institution is taxed by the Federal Government.
- (8) AS 06.30.860 provides an exemption from the state's securities laws. This exemption is unnecessary and redundant. Under the Alaska Securities Act at AS 45.55.140(a)(3), a security issued by state or federal banks or savings associations representing an interest in, or debt of, or guaranteed by the association is exempt from registration under the Act. The appropriate place in the Alaska statutes to state an exemption from the Alaska Securities Act is in the Act itself under Title 45 not under the Banking and Financial Institutions Title (Title 6). No similar language is found in the Alaska Banking Code at AS 06.05.
- (9) AS 06.30.885 provides that obligations to an association contracted prior to the date of enactment of ASAA are enforceable. The statute of limitations has long since run its course in the intervening 17 years. Furthermore, since the first state-chartered savings association application has only recently been approved, the section has no effect and should be repealed.

- (10) AS 06.30.890 provides that the rights and duties matured, penalties incurred, and proceedings begun prior to the effective date of ASAA are not affected. The statute of limitations has long since run its course in the intervening 17 years. Furthermore, since the first state-chartered savings association application has only recently been approved, the section has no effect and should be repealed.
- (11) AS 06.30.900 provides that this chapter is totally controlling on all aspects of savings associations. This drafting approach is to say the least short sighted in that the legislature may at a later time completely change a portion of the law in another chapter or title, e.g., require that security offerings of banks and associations be registered under the Alaska Securities Act, and not think to change AS 06.30.860. The newer pronouncement of the legislature should prevail, however, one does have the loose end of section 900. My recommendation is that section 900 be repealed as an unworkable and ineffective restraint on the legislature's prerogative to enact changes in statutes.
- (12) AS 06.30.905 states that subsequent legislation shall not impliedly repeal provisions of the chapter. My recommendation is that this section be repealed for the reasons stated in discussing the repeal of AS 06.30.900.

In summary, the savings association bill before you is basically a housekeeping measure to aid in the better administration of ASAA and to provide state-chartered savings associations a fair chance to compete with their federal counterparts and other financial institutions for deposits in order to make home loans for Alaskans.

I urge the committee to consider thoughtfully the provisions of the bill. I stand ready to answer any questions that you may have concerning this legislation.

JJB/kfm 5/2

STATE OF ALASKA

JAY S. HAMMOND, GOVERNOR

DEPARTMENT OF COMMERCE & ECONOMIC DEVELOPMENT

DIVISION OF BANKING, SECURITIES, SMALL LOANS & CORPORATIONS

POUCH D - JUNEAU 99811

February 28, 1978

Honorable Joe McKinnon, Chairman
House Commerce Committee
Alaska Legislature
Pouch V
Juneau, Alaska 99811

Dear Mr. McKinnon:

Re: Comments on HB 703

During the course of the past two weeks several questions have been raised concerning various portions of HB 703. I thought it might be helpful to you if I briefly outlined my comments in these matters. The "sec." numbers below refer to the bill section numbers.

Sec. 7. The Federal Home Loan Bank Board has established minimum capitalization requirements in a three-tiered manner, a copy of which is attached. I have no objection to the proposal, from one or more of the member's of the committee, to replace the present two-tier language of the bill with the FHLBB's three-tiered system.

Sec. 15. One or more of the members of the committee questioned the need for the second to the last sentence of AS 06.30.140 found at lines 1-2 on page 15 of the bill. I have no objection to the repeal of that language. However, I suggest that language be inserted to provide for the filling of vacancies on a board between annual meetings, e.g., "If authorized by a vote of the members, vacancies on the board of directors may be filled by a simple majority vote of the remaining directors. [THE DIRECTORS MAY ELECT ALL DIRECTORS]. *appointed me and those persons so*

Sec. 18. Under Sec. 06.30.280(12), the term "hypothecate" is used in addition to the term "pledge." The two terms have similar meanings, i.e., hypothecate means to pledge security but not to transfer possession, while pledge implies a transfer of possession.

Sec. 24. Some question has been raised as to the practicality of Sec. 06.30.445(a), i.e., that a savings association would find it difficult to meet the reserve requirements of the subsection. I suggest that the

Oregon Savings Association Act provision for reserves be used in place of Sec. 445(a) and(c). A copy is attached for your consideration. It appears to be a workable formula and one with which the Oregon Supervisor of Savings Associations has had no trouble.

Sec. 27. The limitations in Sec. 06.30.500(1) on first mortgages found on lines 2-3 of page 24 of the bill were questioned by one or more of the members. The FHLBB regulations on this limitation were recently changed to \$90,000 per unit for Alaska. I would suggest that the pertinent part of lines 2-5 read as follows: "or \$90,000 on a single family dwelling or \$90,000 per unit on a multiple family dwelling ... by regulation." This change should reflect the cost of housing in this State while at the same time provide a prudent guideline for State-chartered savings associations.

The use of the term "regular lending area" in restricting home mortgages under Sec. 06.30.500(5) was also questioned. I see no reason for this restriction and suggest that Sec. 500(5) be deleted. In this way, an association may make loans on property located in the State as provided under Sec. 500(3), which is a reasonable restriction to encourage home mortgage lending in the State.

Sec. 28. The term "regular lending area" is used in Sec. 06.30.505(a)(2). I suggest that Sec. 505(a)(2) be repealed for the reasons stated in the previous paragraph.

Sec. 29. The policy of savings associations making loans on inventory financing of mobile home dealers was questioned by a member of the committee. This sort of financing is provided by banks in this State. If the provision were deleted from Sec. 06.30.505(c) at lines 10-12 of page 26 of the bill, then prospective homeowners in smaller communities may suffer in that mobile homes may not be as readily available on a case by case basis as opposed to a retail sales outlet. The FHLBB allows such financing authority for federally-chartered savings associations.

The reference to Sec. 510 in Sec. 06.30.505 on line 14 of page 26 is correct and should not be changed to Sec. 505. Sec. 510 refers to loans insured through the United States or other political subdivisions and, therefore, should not be included in the restrictions set out in Sec. 505(d).

Sec. 37. The need for provision in State law for the conversion of mutual associations to stock associations was questioned by two witnesses who appeared before the committee on February 23, 1978. Both of those witnesses are associated with a federally-chartered mutual savings association doing business in the State. They further questioned the advisability of such a provision in that the FHLBB has grappled with the conversion issue for some time, without successful resolution, especially the possibility of windfalls to depositors, stockholders, and/or management. Several exhibits were introduced to support their allegations.

My simple response to the issues which were raised by these witnesses concerning conversion is that there is a need for the provision in State

law. More than 30 states have provided for stock savings associations and have not been intimidated by the alleged failure at the federal level to resolve the issue of conversion.

I use the word "alleged" because my discussions with officials of the FHLBB, both in the Seattle regional office and in Washington, D. C., as well as discussions with Mr. William Bergman, Executive Director of the National Association of State Savings & Loan Administrators, and Frank Gailor, general counsel for NASS & LA, indicate that they believe that the FHLBB regulations have proven to be sound and have protected depositors, customers, and stockholders involved in conversions.

Congress provided for a period during which FHLBB could process applications from federally-chartered mutual associations to convert to federally-chartered stock associations. That law expired June 30, 1976. The FHLBB received upwards of 90 applications prior to that date and was not able to complete all of them before that date. The result has been a disagreement between Senator Proxmire of the Senate Banking Committee who maintains, based on a GAO audit that FHLBB no longer has authority to process the applications, and FHLBB which holds the contrary. This controversy is what is reported in the American Banker article of July 21, 1977. There has never been a controversy over the authority of the State to enact legislation to allow savings associations to convert from mutual to stock organizations. Furthermore, the article in the American Banker of August 12, 1977, reported by Kenneth Virch should be read in context. That is, Mr. Virch is associated with the Council of Mutual Savings Institutions, an organization whose primary purpose in the estimation of Mr. Gailor (see NASS & LA's testimony in support of HB 703 dated February 14, 1978) is to lobby against provisions for stock savings associations.

In summary, it is the considered opinion of a number of officials of FHLBB that the "experiment" to allow conversions of federal mutuals to federal stock associations was a success, that the benefits of converting to stock associations are obvious in that it injects additional capital into the association which can in turn be used to make more loans to prospective homeowners, that the regulations adopted by the FHLBB have proven adequate and that no evidence has been presented of cases where insiders or others have enjoyed windfalls due to conversions.

The two witnesses cautioned against provision in state law for conversions because the matter is extremely complex and should be studied, e.g., by the Alaska League of Savings and Loan Associations, before the Legislature acts. However, I would draw your attention to the proposed language of Sec. 06.30.776 which provides that the commissioner "may provide by regulation for the procedure to be followed in the conversion." Perhaps the word should be "shall" rather than "may." In any case, it is very likely that the department would look closely to the proven regulations which the FHLBB has already adopted in this area, i.e., 12 CFR 563.b, a copy of which was supplied to the committee by Mr. Eddie Turner. Those regulations would very likely have to be followed in a conversion anyway. Those regulations set out a reasonable procedure for conversion that has in fact

worked in 30 cases. See for example the "Notice of Special Meeting of Members, Proxy Statement and Plan of Conversion to a Federally Chartered Stock Association" for First Federal Savings & Loan of Fresno submitted by Mr. Turner.

The FHLBB regulation at 12CFR 563.b provides detailed guidelines for conversion. They include the requirement that the reserve account of the mutual must be made a separate portion of the net worth of the newly converted stock association and that upon liquidation of the stock association at some time in the future, the depositors of record on the date of conversion shall have priority to the extent of that net worth and receive a pro rata share of it.

For example, assume one has a \$100 million mutual savings association with a reserve account of \$5 million which is to be converted to a stock association. Assume further that \$6 million in stock subscriptions are sold. The association is converted and has a net worth of \$11 million. Assume it operates for one day, has no earnings and liquidates. The depositors at the date of conversion would get back pro rata portions of the \$5 million and the stockholders would have priority on return of the balance of the net worth of the association, i.e., \$6 million.

In this way there is no windfall to the stockholders of the stock association or to its management. Furthermore, purchase of shares in the new stock association is limited. That is, each depositor at the time of conversion is entitled to a pro rata right to purchase stock plus ten times that amount. Management is entitled to a similar purchase up to fifteen times their pro rata right. There has been no showing or evidence in the view of officials of FHLBB that these provisions have been abused. Furthermore, Mr. Douglas Faucette, Director of the Securities Division within the Office of General Counsel of FHLBB in Washington, D. C., stated to me that no accusations have been filed by FHLBB against any person pursuant to the 30 conversions that have been processed alleging windfall profits as a result of those conversions.

In addition to the federal regulations, the commissioner could look to such provisions as appear in the Oregon Savings Association Act at ORS 722.064, a copy of which is attached. They set out a procedure that supplements the FHLBB's regulations.

In summary, then, there is no reason for the Alaska Legislature to delay in providing for stock savings associations in this State. There is certainly no reason to delay in providing for conversion from a mutual to a stock association. The FHLBB experiment has shown the great amount of interest in conversion by federal associations and also that those conver-

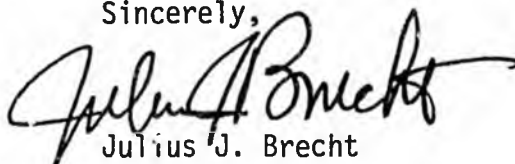
February 28, 1978

sions can be accomplished without windfalls and in the best interest of the depositors, new stockholders, management, and old and new customers of the stock association.

A prime example of the potential gain to Alaskan homeowners is the experience of American Savings & Loan of Miami Beach, which went from \$250 million to \$500 million in assets within two years of conversion. This information was obtained from the Director of the Securities Division within the Office of General Counsel of FHLBB in Washington, D. C.

I would, therefore, urge you and the committee to consider thoughtfully the ramifications of not providing for stock associations in this State and, furthermore, the possible stifling effect on the growth of the savings association industry in this State by not allowing for conversion of mutual associations to stock associations. I stand ready to discuss this bill further at your convenience.

Sincerely,



Julius J. Brecht
Director

Enclosures

JJB:1c4:15

Minimum Capital Requirements
Applicants for Insurance of Accounts

and

Permission to Organize a Federal S&LA

| <u>Population of Area</u> <u>1/</u> | <u>Stock Applicant</u> | | <u>Mutual Applicant</u> |
|-------------------------------------|--|--|--|
| | <u>Total Stock and Paid-in Surplus</u> <u>2/</u> | <u>Amount of With-drawable Savings</u> <u>3/</u> | <u>Amount of With-drawable Savings</u> <u>4/</u> |
| Under 25,000 | \$500,000 (100) | \$250,000 (175) | \$500,000 (350) |
| 25,001 - 100,000 | \$1,000,000 (200) | \$500,000 (350) | \$1,000,000 (750) |
| Above 100,000 | \$2,000,000 (400) | \$1,000,000 (700) | \$2,000,000 (1,000) |

This schedule is only a minimum and the Board may impose higher requirements to reflect likely savings growth, operating results and other factors relating to the risk exposure to the Insurance Corporation.

- 1/ In determining population, the area will be defined as the SMSA, if the association is located in an SMSA. In a non-SMSA, the population will be based on the delineated service area or the county in which the association is located, whichever is greater.
- 2/ Generally, the amount of paid-in surplus should be approximately 20 percent of the amount of permanent stock required. The figures in parenthesis indicate the minimum number of stockholders.
- 3/ The figures in parenthesis indicate the minimum number of subscribers to withdrawable accounts. The association will be required to raise 50% of the amount in cash prior to the granting of final approval of insurance and the remainder within 60 days of the granting of insurance.
- 4/ The association will be required to raise 100% of the amount in cash prior to the granting of final approval of insurance. The association will also be required to pledge 20% of the amount or \$250,000, whichever is less, with the FHLB as a guarantee against operating deficits. The figures in parenthesis indicate the minimum number of subscribers to withdrawable accounts.

722.142 General reserve for losses and net worth requirements. (1) A savings association shall establish and maintain a general reserve account for losses and other net worth accounts adequate to assure solvency of the association.

(2) (a) Each savings association shall accumulate and maintain as a net worth account a general reserve for the sole purpose of absorbing losses. At the annual closing date following the anniversary of its certificate of authority and each annual closing date thereafter, the general reserve shall have a minimum balance not less than an amount fixed by rule.

(b) The supervisor by rule shall fix the required minimum amount of general reserve accounts of associations. The rule shall provide a uniform schedule of minimum levels to be reached during the first 20 or more years of an association's operation for the purpose of achieving an orderly accumulation of the general reserve account.

(3) The supervisor may permit an association to cure a deficiency in its general reserve account by requiring the board of directors of the association to earmark earned surplus, voluntarily pledged savings accounts of a mutual association, or capital surplus or stated capital of a stock association, as part of its general reserve account in the amounts needed to cure the deficiency. Amounts so earmarked shall be held for the same purpose as the general reserve to the extent the earmarked amounts are needed to maintain the required reserve account level. An association shall not pay dividends or interest from the reserve account or other funds earmarked for the purpose of meeting the reserve account requirement.

(4) Every savings association shall build up and maintain its net worth so that at the close of business on any annual closing date its net worth accounts shall equal not less than the dollar amount determined in accordance with the rules to be adequate to assure solvency of the association. The rules shall provide for an adjustment of the net worth requirement during the first years of an association's operation in accordance with paragraph (b) of subsection (2) of this section. If an association fails to establish or maintain the general reserve or the net worth requirements of this section, the supervisor may in accordance with ORS 722.464 require the association to take appropriate corrective action.

(5) An association may establish reserve accounts, in addition to the general reserve, as its board of directors may authorize, and

make transfers to and charge such reserve accounts.

(6) Losses as they are determined, not charged to other reserve accounts, shall be charged to the general reserve until the general reserve account is exhausted. After exhaustion of the general reserve, any remaining losses not charged to other reserve accounts shall be charged as determined:

(a) In the case of a stock association, to earned surplus, then capital surplus and then stated capital; or

(b) In the case of a mutual association, to earned surplus and then the expense fund, if any.

(7) Any insurance reserve required by an insurer of the savings accounts of an association shall be considered part of the general reserve for the purpose of subsection (2) of this section.

TESTIMONY OF JULIUS J. BRECHT, DIRECTOR
DIVISION OF BANKING & SECURITIES
DEPARTMENT OF COMMERCE & ECONOMIC DEVELOPMENT
BEFORE
HOUSE COMMERCE COMMITTEE

February 6, 1978

Good morning, Mr. Chairman and members of the committee. My name is Julius J. Brecht, and I am Director of Banking & Securities within the Department of Commerce & Economic Development. I want to thank you for allowing me to appear before you to offer comment on HB 703.

As you know, this bill makes several changes to the Alaska Savings Association Act (ASAA), AS 06.30. The ASAA was enacted in 1961 and provides for the chartering of savings and loan associations whose primary service is home mortgage lending to the Alaskan public. The ASAA has had little revision since that time. However, in the intervening 17 years, major changes have been made in the federal law and regulations affecting federally-chartered savings associations. As a result, institutions chartered under ASAA are at a decided disadvantage in the financial marketplace. The net effect is that a state-chartered association would find it very difficult to compete with its federally-chartered counterparts. There is, however, renewed interest in state-chartered savings associations.

I, therefore, concur with the sponsor of this bill that a comprehensive review of ASAA is in order. The bill before this committee is the result of such a review, coordinated between the sponsor and the Division of Banking & Securities.

I have had the following documents distributed to members of the committee for their information:

1. a memorandum dated December 28, 1977, which gives a section-by-section analysis of the bill;
2. a fiscal note prepared by myself dated February 2, 1978, and
3. a copy of a written statement of testimony before this committee.

Those documents will give a detailed analysis of the provisions of the bill. However, the major provisions of the bill include:

1. revised association chartering procedures;
2. revised branch, agency, and change of location application procedures;

3. provisions for the establishment of stock savings associations;
4. procedures for the conversion from a mutual savings association to a stock association;
5. provision for fixed interest savings accounts; and
6. provisions to update lending requirements.

A number of the proposed changes are based on proposed changes to the Alaska Banking Code found in SB98, e.g., the chartering and branching procedures. The division will then be using a common procedure, when appropriate, in dealing with new bank or new savings association applications or branch applications from banks or associations and thereby allow for timely processing of applications in the best interest of the applicant, the institution, and the Alaska taxpayer.

A number of the proposed changes are based on the present Alaska Banking Code, e.g., reserves for bad debts, filing fees, inactive accounts, and conditions on the submission of annual reports. A number of the proposed changes come from the recently recodified Savings Association Act of the State of Oregon, e.g., incorporation procedure, bylaws, certificate of authority, conditions on the payment of dividends, second liens, and service corporations. A number of the changes are based on the federal law and regulations of the Federal Home Loan Bank Board, e.g., minimum capital requirements and fixed rate of interest accounts.

The bill has been reviewed by the staff of the Federal Home Loan Bank, the federal insurer of accounts of both federal and state-chartered savings associations in this State. While the federal agency cannot offer official comment on the bill, I have been informed that the staff of that federal agency in Seattle sees no conflict between the provisions of the bill and federal laws or regulations. In addition, the bill has been reviewed by representatives of an association that has recently been given conditional approval to incorporate as a state-chartered savings association. They are in full support of all of the provisions of the bill.

In summary, the bill before this committee is basically a long overdue housekeeping measure. It will aid in the better administration of ASAA and provide state-chartered savings associations a fair chance to compete with their federal counterparts and other financial institutions. The bill will inject competition into the financial marketplace and thereby ensure better service to Alaskans seeking home loans.

I, therefore, support the provisions of the bill and stand ready to answer any questions that the Committee may have.

To: The House Commerce Committee

From: Eddie J. Turner

Subject: House Bill 703

It appears that the one area of concern regarding HR 703 is competitive competition.

Competitive competition is the American way of life in business and is good for the consumer customer. It allows a freedom of choice as to where to deposit their savings and where to secure a mortgage loan for their home or business.

Freedom of choice has been very limited to residents outside of a metropolitan trade area and for a long time this was true of all residents of Alaska, as they were dependent on Seattle, Washington for most all of their needs.

We have progressed beyond this step-child era to a mature statehood status and it is difficult for some to realize or accept this true fact that our wants, needs and desires are no different than residents of other states in this United States of America.

Profits are the measurement of success or failure in a free enterprise economy.

The Federal Insurance Reserve requirements for a Federal Association establishes only the minimum amount and the Federal Supervisory Authorities encourage Federal Associations to exceed this amount and have stronger reserves for the protection of the account holders and members. One association, First Federal Savings of Anchorage has approximately 10% in reserves, almost double the minimum requirement of 5% after 20 years. A draft of HR 703 has been reviewed by the Federal Home Loan Bank of Seattle and in my discussions with them, they commented only on the reserve requirements being excessive.

Overall, the bill that you are now considering is very comprehensive and thorough and Mr. Brecht and his staff should be commended for their efforts. We have received excellent cooperation from this Department. My main concern about the context of HR 703 is from an operational point of view that we can be competitive with our Federal counterparts and compatible with the other financial institutions in the State of Alaska. Mr. Brecht has to also view the context of HR 703 from a supervisory aspect in addition to operational. I feel that we are in agreement with nearly every section of this bill. In addition, I have researched, studied and compared the State Statutes of nearly 15 other States, including Washington, Oregon, California, Arizona and Hawaii, and have determined to my satisfaction that HR 703 is comparable to the other State Statutes and is not at variance with Federal Statutes and Regulations.

House Bill No. 703
"An Act relating to Savings Associations"

In 1961, Chapter 30 of the Banks and Financial Institutions Statutes titled the Alaska Savings Association Act was enacted. The basic context was from a model savings and loan act formulated by the United States Savings and Loan League. Since that time, the statutes have not been updated and modernized to allow a State Savings and Loan to be competitive with its Federal counterparts.

As a matter of sound public policy, there should be both state and federally chartered savings and loans and each should have the option to choose between the mutual and stock forms of ownership in keeping with our free enterprise economic system.

Thirty states currently have stock savings and loan associations and this year there are four other states besides Alaska considering stock legislation.

Prior to 1975, all Federal Associations were mutually owned and could only convert to a state stock association. In 1975, a federal stock charter for federal associations was developed by their regulatory authorities because they felt it was important that associations have the ability to choose freely the form of organization under which they wish to operate.

The proposed changes in the Alaska Savings Association Act are parallel in many respects to the Federal Regulations because of FSLIC Insurance of Accounts requirements.

A local savings and loan association, organized to serve the surrounding community, can best provide for the promotion of savings and economical home financing to the unserved or underserved residents because of the involvement in community affairs.

It is therefore very important that the residents of Alaska be given the freedom of choice in their investment of funds.

Stock Conversions
Where are we now.

Reason for permitting conversions:

As a matter of sound public policy, both State and Federally chartered savings and loan associations should have the option to choose between the mutual and stock forms of ownership.

- (1) Increased equity base to support savings growth.
- (2) Additional funds for housing.
- (3) Beneficial effect on industry structure.
- (4) Fostering of faster growth and more effective competition.
- (5) Forestalling supervisory action.
- (6) Fostering sound and aggressive performance.
- (7) Allowing Freedom of choice.

The Federal Home Loan Bank's sale-of-stock regulations are designed to eliminate the windfall aspect of conversion, while providing the accountholder with the right to a share in the equity of the converting mutual association in the event of a subsequent complete liquidation.

Conversion has no effect on insurance of savings accounts.

In a converted stock association, exclusive voting rights are in the stockholders unless, in the case of State-chartered stock associations, State law requires otherwise. This change in voting rights has only a minor effect on accountholders, since most accountholders in a mutual association sign proxies of indefinite duration at the time their savings accounts are opened and these permit one or more directors of the association to exercise the accountholders' voting rights.

Stock Conversions— Where We Are Now

by Charles E. Allen

This report will describe the status of mutual to stock conversions of federally insured savings and loan associations as of February 15, 1976. It also will discuss the reasons why associations need to have the option to convert on a sale-of-stock basis. In addition, it will summarize the Federal statutory provisions and the regulations of the Federal Home Loan Bank Board which permit conversions on a sale-of-stock basis.

Current Filings

The Board has received 43 mutual to stock conversion applications from savings and loan associations in the following States: 9 from Florida; 8 from California; 6 from Texas; 2 each from Arizona, Colorado, Illinois, Maryland, New Jersey, and Wisconsin; and 1 each from Kansas, Michigan, Mississippi, Ohio, New Mexico, Tennessee, Utah, and Washington. Of the 43 associations applying to convert, 35 are federally chartered associations and 10 are State-chartered. Based on total asset size, 7 of the conversion applicants have assets in excess of \$500 million, 12 between \$100 million and \$500 million, 7 between \$50 million and \$100 million, and 17 less than \$50 million.

Eleven associations have amended their conversion applications under the Board's revised sale-of-stock regulations which became effective in June 1975. This includes one association converting on a free distribution basis in accordance with a statutory grandfather provision, but otherwise complying with these regulations. In addition, six associations have filed original conversion applications under the revised regulations. Of these 13 conversion applications, 7 have been approved by the Board and the other 11 are being processed. The timing of application processing by the Board is primarily dependent on the actions of the converting association. There has been no significant delay attributable to the Board or its staff in processing conversion applications under the revised regulations.

Of the 25 applications which have not been amended under the revised conversion regulations, 15 associations plan to file amended applications, 8 have not advised the Board whether they intend to proceed, and 2 plan to withdraw their conversion applications. In addition, a number of associations have informally indicated that they are in the

Enron's Note: Mr. Allen, who had been General Counsel for the Board from May 1972 until his recent return to private law practice, had written this article for the Journal before his resignation.

process of preparing sale-of-stock conversion applications. These include several minority associations.

Approved Conversions

On October 10, 1975, the Board approved the first mutual to stock conversion of a savings and loan association under its sale-of-stock regulations. The Board has now approved six conversions involving a sale of stock. These conversions are demonstrating the workability and desirability of the Board's sale-of-stock approach in this matter and are materially increasing the net worth of the converting associations without a windfall to any group. At the same time, no association is being forced to convert.

The Board also has approved a free distribution conversion of one of three associations entitled, on a grandfather basis, to convert without a sale of stock in accordance with a Congressionally mandated provision in the National Housing Act. Of the other two grandfathered associations, one is expected to amend its conversion application and the other to withdraw.

Reasons for Permitting Conversions

As a matter of sound public policy, both State and federally chartered savings and loan associations should have the option to choose between the mutual and stock forms of ownership. The primary reasons for allowing such a choice include the following:

(1) Increased equity base to support savings deposit growth. In the savings and loan industry, equity capital is critical because of its ability to provide leverage for increased deposit growth. Based on a Federal insurance reserve requirement of 5 percent of savings deposits, \$1.00 in new equity capital can support \$20.00 in new deposits for home mortgage lending and other services. Mutual associations can increase their equity base only out of retained earnings. In geographical areas of rapid growth and greatest housing needs, retained earnings are often inadequate to provide the equity base to support the available increase in savings deposits. Hence, the financing of housing—the primary function of savings and loan associations—is not fully provided without the potential to convert.

Although the Board has allowed long-term subordinated debentures issued under section 563.8-1 of the Insurance Regulations to meet up to 20 percent of the net worth requirement of section 563.13(b), it has, as a matter of policy, consistently rejected requests to permit such debentures to be used to satisfy any part of the Federal insurance

reserve requirement of section 563.13(a), which is based on section 403(b) of the National Housing Act. There also is substantial doubt as to whether the Board has authority under the statute to do so. Debentures of this type cannot be regarded as equity capital against which losses can be charged, but are debt that must be repaid at maturity and that usually bears a rate of interest that severely limits its usefulness.

(2) Additional funds for housing. The sale of capital stock provides additional funds that otherwise would not be invested in S&L's. In the case of larger associations, the sale of stock also provides a device to obtain additional funds from other areas. These additional funds will increase an association's ability to make more housing loans.

(3) Beneficial effect on industry structure. The sale of capital stock operates to improve the efficiency of the S&L industry. For example, the merging of mutual associations often can be complicated by their unequal net worth positions if one association is contributing more resources to the proposed merger than the other. In contrast with the case of mutual associations, differences in the valuation of stock institutions are made quite manageable simply by pricing the stocks relative to their proportionate contribution to the merger.

(4) Fostering of faster growth and more effective competition. The sale of capital stock has additional advantages from a competitive standpoint—a factor of major importance because of the substantially increased competition between S&L associations and commercial banks since the early 1960's and because of the growing complexity of S&L operations. Stock associations, for instance, are able to offer additional means for attracting and compensating, through stock option plans more skilled and more aggressive S&L managers.

(5) Forestalling supervisory action. The ability to raise common stock equity capital is especially important in forestalling supervisory action. One of the principal reasons for the weakness of some associations and the need for supervisory action is the inadequacy of net worth to absorb writedowns of bad loans and foreclosed real estate. The supervisory situation is improved, moreover, by the existence of a body of stockholders who have their funds at risk and who form a clear and explicit group to whom the management is responsible for sound and proper performance.

(6) Fostering sound and aggressive performance. In the past, there has been some aversion to con-

versions of mutuals to stock associations because of a belief in the unsoundness of the practices of some stock associations. It has been shown, however, that the operating differences between the stock and mutual forms of organization are not great. Stock associations appear to exhibit a faster rate of growth, are somewhat more profitable over the long run, and possibly have lower cost ratios when other factors are held constant. They do appear to incur a somewhat higher level of risk than mutual associations, although factors other than the form of or-

ganization appear most important in determining the degree of risk.

(7) *Allowing freedom of choice.* From the public policy standpoint, and in keeping with our free enterprise economic system, it is important that associations have the ability to choose freely the form of organization under which they wish to operate. Since conversions can be accomplished in a safe and equitable manner under the Board's sale-of-stock regulations, there is no need to restrict associations to the mutual form of organization. This is especially true for federally or State-chartered associations in States which allow S&L's to operate in either the mutual or stock form.

Statutory Provisions

Conversion of Federal mutual associations to the stock form of ownership is permitted on an equitable basis under the third unnumbered paragraph of section 5(i) of the Home Owners' Loan Act. The first sentence of paragraph (3) of section 402(j)

J. Ralph Stone Nominated as FHLBB Member



J. Ralph Stone, of Santa Rosa, Calif., a California savings and loan association executive, was nominated by President Ford on February 6 to be a Member of the Federal Home Loan Bank Board.

Mr. Stone was named by the President to succeed former Board Chairman Thomas R. Bomar, who resigned as of June 20, 1975, to become president and managing officer of American Savings and Loan Association of Miami Beach, Fla.

Mr. Bomar's term would have expired on June 30, 1978. A hearing on Mr. Stone's nomination was held by the Senate Banking, Housing, and Urban Affairs Committee on March 1.

Board Member Garth Marston, a Republican, has been Acting Chairman of the Federal Home Loan Bank Board since being named to that post by President Ford on July 7, 1975. The Board's third Member is Grady Perry, Jr., a Democrat.

At the time of his nomination, Mr. Stone was executive vice president of Great Western Savings

and Loan Association, of Beverly Hills, Calif., and vice president of Great Western Financial Corporation. Previously, he was a director, president, and chairman of the board of Santa Rosa Savings and Loan Association, serving successively in those positions beginning in 1948. He was named executive vice president of Great Western in 1968 when that association bought out Santa Rosa Savings and Loan Association.

Born in Sebastopol, Calif., on June 11, 1910, Mr. Stone was graduated from the University of California at Berkeley with a B.A. degree in economics in 1931 and became a partner in a retail furniture establishment, a connection he still maintains. From 1961 to 1967, he was a director of the California Savings and Loan League, serving as vice president from 1966 to 1967 and as president from 1967 to 1968. He was chairman of the capital stock committee of the United States Saving and Loan League from 1967 to 1968 and has been a member of the League's legislative committee since 1962.

Mr. Stone was elected a director of the Federal Home Loan Bank of San Francisco in 1968 and was twice reelected to that post in 1970 and 1972. In 1975, he was named chairman of the Advisory Committee to the President of the Bank.

of the National Housing Act permits a converting Federal mutual association to retain its Federal charter. However, the second sentence of paragraph (3) prevents the Board from permitting the conversion of Federal mutual associations to the stock form in States not authorizing the operation of State-chartered stock associations, except in the District of Columbia, Puerto Rico, or States in which all federally insured associations are federally chartered. Section 402(j) also recognizes the Board's authority over the conversion of State-chartered mutual institutions to the stock form.

Section 402(j) imposes a limited statutory moratorium—which expires on June 30, 1976—on non-supervisory conversions. Before this date, the Board is authorized to approve 43 conversion applications, plus 8 applications that had been submitted for filing before May 22, 1973. There is no limitation on the number of conversion applications which the Board may approve after June 30, 1976, but the other provisions of section 402(j) continue in effect. These provisions include factors to be considered in putting conversions into effect and a requirement to report annually to Congress on the exercise of the Board's conversion authority.

Section 402(j) supports the Board's sale-of-stock approach to conversions and makes specific reference to the Board's conversion regulations, which at the time of the amendment of section 402(j), in Octo-

ber 1974, already required this method of conversion. Section 402(j) also recognizes the sale-of-stock requirement by providing a grandfather exception from this requirement for three Federal associations which had given written public notice to their accountholders, before May 22, 1973, of adoption of a free stock distribution plan of conversion. This statutory exception permits a free distribution to accountholders of such associations only as of a record date that is prior to the date of the public notice.

Paragraph (4) of subsection 402(j) limits judicial review of the Board's final approval of a plan of conversion to a petition in the appropriate United States Court of Appeals. The petition must be filed within 30 days of the later of (1) the mailing of the proxy statement or (2) publication in the Federal Register of notice of the Board's final approval.

Regulatory Provisions

The Board has determined that a method of conversion which provides a so-called windfall distribution of stock to accountholders of a converting mutual savings and loan association would create strong incentives for significant shifts of savings funds from other associations and that these shifts would unacceptably threaten the financial stability of these associations. The Board also has determined that a method of conversion which provides a

The following table sets forth certain information with respect to the approval of the plan of conversion by the Board and by the members of the converting association and information concerning the subscription offering.

| Name | Date of FHLBB approval | Date of members meeting | Votes cast in favor | Votes cast against | Dates of subscription offering | Percentage of shares sold in subscription offering |
|--|-----------------------------|-------------------------|---------------------|--------------------|--------------------------------|--|
| Franklin Savings Association (Austin, Tex.) | 10/10/75 | 11/03/75 | 89,969 (61.3%) | 4,019 (2.7%) | 11/20/75 to 12/15/75 | 100% to account holders and borrowers |
| American Savings and Loan Association of Florida (Miami Beach, Fla.) | 11/3/75 (amendment 2/4/76) | 12/17/75 | 725,123 (60.7%) | 109,199 (9.1%) | 2/6/76 to 3/4/76 | (¹) |
| Sweetwater Savings Association (Sweetwater, Tex.) | 12/3/75 | 1/30/76 | 182,550 (58.2%) | 7,868 (2.6%) | 2/10/76 to 3/6/76 | (¹) |
| Standard Federal Savings & Loan Association (Guthrieburg, Md.) | 12/19/75 | 1/28/76 | 282,716 (56.7%) | 36,981 (7.4%) | 2/6/76 to 3/2/76 | (¹) |
| First Federal Savings & Loan Association of Fresno (Calif.) | 12/19/75 | 1/28/76 | 725,063 (72.9%) | 32,287 (3.2%) | 1/30/76 to 2/19/76 | (¹) |
| Prudential Federal Savings & Loan Association of Salt Lake City (Utah) | 12/19/75 (amendment 1/9/76) | 3/5/76 | — | — | (¹) | (¹) |
| First Federal Savings & Loan Association of Conroe (Tex.) | 2/4/76 | 2/27/76 | — | — | — | (¹) |

¹ Underwritten public offering of any unsubscribed shares.
² Management syndicated to purchase any unsubscribed shares.
³ Free distribution conversion; subscription offering of shares to

be sold for the accounts of depositors allocated fewer than 100 shares who elect to have their shares sold.

windfall distribution would tend to force individual mutual associations to convert to the stock form irrespective of whether they, or the communities they serve, would be benefited thereby. The Board therefore found that no method of conversion can be considered equitable unless windfall distributions are eliminated. These findings were based, to a significant extent, on a study entitled "The Impact of 'Free Distribution' Conversion Windfalls on the Savings and Loan Industry" dated February 28, 1974, and prepared by the Board's Office of Economic Research. Copies of this study are available to the public.

Thus, the Board's sale-of-stock conversion regulations are designed to eliminate the windfall aspect of conversion, while providing the account holder with the right to a share in the equity of the converting mutual association in the event of a subse-

quent complete liquidation. Here are some of the principal provisions of these regulations:

1. **Approval of Plan of Conversion.** The plan of conversion must be approved by a two-thirds vote of the board of directors of the converting association and by a majority of all votes eligible to be cast at a meeting of members called for that purpose. Only proxies solicited for this purpose may be voted. A proxy statement making full Securities and Exchange Commission type disclosure is required for soliciting proxies. Final approval of the plan by the Board is required before soliciting proxies.

2. **Plan of Conversion.** The plan of conversion must provide for a sale of all shares of capital stock being issued at a total price equal to the estimated pro forma market value of the shares, based on an independent appraisal. Each eligible account holder must receive, without payment, nontransferable subscription rights to purchase the greater of 10 times his pro rata portion of the total shares being sold or 100 shares. In the event of an oversubscription by eligible account holders, shares would be allocated primarily on a pro rata basis, based on qualifying deposits. An eligible account holder is a savings account holder on the eligibility record date, which must be at least 90 days before adoption of the plan

The following table summarizes certain financial information concerning each converting association whose plan of conversion has been approved by the Board.

| Name | Asset size | Net worth ^a | Pro forma net worth ^b | Net income | Pro forma net income |
|---|---------------|------------------------|---|----------------------|---|
| Franklin Savings Association (Austin, Tex.) ¹ | \$ 33,565,000 | \$ 413,000 (1.45%) | \$ 1,583,000 or \$7.43 per share (5.56%) | \$ 103,000 (9 mos.) | \$ 173,000 or \$ 8 ¹ / ₂ per share (9 mos.) |
| American Savings and Loan Association of Florida (Miami Beach, Fla.) ² | \$454,471,000 | \$14,064,000 (3.6%) | \$20,603,000 or \$41.20 per share (5.3%) | \$1,420,000 | \$1,803,000 or \$3.62 per share |
| Sweetwater Savings Association (Sweetwater, Tex.) ¹ | \$ 34,623,000 | \$ 1,294,000 (4.4%) | \$ 1,894,000 or \$22.99 per share (6.4%) | \$ 79,000 | \$ 116,000 or \$1.41 per share |
| Standard Federal Savings & Loan Association (Gaithersburg, Md.) ¹ | \$ 53,974,000 | \$ 746,000 (1.50%) | \$ 2,396,000 or \$9.58 per share (4.83%) | \$ 253,000 | \$ 352,000 or \$1.41 per share |
| First Federal Savings & Loan Association of Fresno (Calif.) ² | \$124,232,000 | \$ 3,712,000 (3.6%) | \$ 6,037,000 or \$13.74 per share (5.8%) | \$ 431,000 | \$ 593,181 or \$1.35 per share |
| Prudential Federal Savings and Loan Association of Salt Lake City (Utah) ¹ | \$507,095,000 | \$29,966,000 (8.4%) | \$29,106,000 or \$11.41 per share (8.1%) | \$2,774,000 (9 mos.) | \$2,774,000 or \$1.09 per share (9 mos.) |
| First Federal Savings and Loan Association of Conroe (Tex.) ¹ | \$ 37,560,000 | \$ 1,676,000 (5.04%) | \$ 2,556,000 or \$19.36 per share (7.68%) | \$ 130,000 | \$ 199,000 or \$1.43 per share |

¹ Asset and net worth at June 30, 1975, and net income for the 9 months then ended.

² Asset and net worth at December 31, 1975, and net income for the year ended September 30, 1975; net income was \$351,000 for the 3 months ended December 31, 1975. Pro forma and net proceeds calculations are based on \$14.50 per share, the maximum price in the \$10.72 to \$14.50 price range; such calculations assume a sale of all shares in the subscription offering, and therefore do not include underwriting commissions of up to 8 percent of the offering price.

³ Asset and net worth at September 30, 1975, and net income for the year then ended.

⁴ Asset and net worth at September 30, 1975, and net income for the year ended June 30, 1975; net income was \$81,000 for the 3 months ended September 30, 1975.

⁵ Asset and net worth at October 31, 1975, and net income for the year ended June 30, 1975; net income was \$276,000 for the 4 months ended October 31, 1975. Pro forma and net proceeds calculations are based on \$5.80 per share which is the average price within the \$5.01 to \$6.60 price range.

⁶ Asset and net worth at September 30, 1975, and net income for the 9 months then ended. Pro forma net worth reflects estimated conversion costs, but not any payments in respect to fractional shares or supplemental payments which as a maximum

by the board of directors of the converting association. Qualifying deposits refer to the savings accounts of an eligible accountholder on the record date. An eligible accountholder's pro rata portion is determined by multiplying the total number of shares to be sold by a fraction of which the numerator is the amount of his qualifying deposit and the denominator is the total amount of qualifying deposits of all eligible accountholders.

Plans of conversion may provide, as part of the subscription offering, for shares not purchased by eligible accountholders to be offered to directors, officers, and employees up to 20 percent of the total offering in the case of converting associations with total assets of less than \$50 million—with this percentage decreasing to 10 percent in the case of an association with total assets of more than \$500 million.

All shares not purchased in the subscription offering must be sold. The plan of conversion may provide for these unsubscribed shares to be offered to those eligible accountholders desiring to purchase more than 10 times their pro rata portion or to other accountholders and borrowers. The unsubscribed shares also may be sold in a public, underwritten offering or in a private distribution that

includes a management syndicate. If unsubscribed shares are to be sold in a private distribution, the plan must provide eligible accountholders with subscription rights of 15 times, rather than 10 times, their pro rata portion of the shares being sold. If shares are to be sold in a private distribution, the plan also must provide for each accountholder and borrower to be offered up to 100 shares before the sale.

A converting association may, in its plan of conversion, limit the number of shares being purchased in the subscription offering by an eligible accountholder, or any group of eligible accountholders acting in concert, to 1 percent of the total offering. The plan also may require a minimum purchase of 25 shares.

The plan of conversion must provide for a sale of the shares without any discount from the pro forma market price established by the independent appraisal. The plan must also provide that all shares purchased by directors or officers as part of the subscription offering or otherwise in connection with the conversion not be sold for a period of 1 year and that the stock certificates be so legended.

Conversion has no effect on insurance of savings accounts. The plan of conversion must provide for continued Federal insurance of savings accounts and membership in the Federal Home Loan Bank System. A plan of conversion has no effect on savings account balances, interest rates, or maturities. An accountholder continues to have the same account in the converted stock association as he had before the conversion in the mutual association. The only differences are with respect to voting and liquidation rights.

In a converted stock association, exclusive voting rights are in the stockholders unless, in the case of State-chartered stock associations, State law requires otherwise. This change in voting rights has only a minor effect on accountholders, since most accountholders in a mutual association sign proxies of indefinite duration at the time their savings accounts are opened and these permit one or more directors of the association to exercise the accountholders' voting rights.

A converting association must create a liquidation account in an amount equal to the net worth of the association at the latest practicable date before conversion. Each eligible accountholder has a pro rata inchoate interest in a portion of the liquidation amount based on the amount of his qualifying deposits on the eligibility record date. His proportionate interest cannot increase, but will be reduced by a subsequent decrease in his deposit balance. The function of the liquidation amount is to establish a priority on liquidation, and not to otherwise

| Number of shares | Price per share | Estimated net proceeds | Proposed quarterly cash dividend |
|------------------|----------------------|------------------------|----------------------------------|
| 213,333 | \$ 6.00 | \$1,170,000 | None |
| 500,000 | \$14.50 (maximum) | \$6,539,000 | \$.19 per share |
| 82,353 | \$ 8.50 | \$ 600,000 | None |
| 250,000 | \$ 7.00 | \$1,650,000 | None |
| 439,394 | \$ 5.80 (average) | \$2,325,000 | \$.08 per share |
| 2,552,000 | (Free distribution) | | \$.06 per share |
| 132,000 | \$ 7.50 | \$ 880,000 | |

would reduce pro forma net worth to \$11.21 per share. At January 5, 1976, appraisal indicated market value range of \$11,561,000 to \$15,644,000 or \$4.53 to \$6.13 per share.

* Asset and net worth at September 30, 1975, and net income for the year then ended.

** Net worth and pro forma net worth are shown as percentages of savings.

NOTE: The above financial information is based on financial statements (some of which are unaudited) and other financial data contained in the proxy statement and/or offering circular of the converting association.

restrict the use or application of any of the net worth accounts of the converted association. No payment to the account holder would be made except in the case of a complete liquidation of the association. A merger or sale of assets in which savings accounts and other liabilities are assumed by the surviving association would not be viewed as a complete liquidation for this purpose, and the liquidation amount would be assumed by the surviving association.

A converting association must enter into an agreement with the Board that, for a 3-year period following conversion, no company engaged in an unrelated business activity shall be permitted to acquire control of the association. A similar charter provision without the 3-year time period is optional for State-chartered associations and mandatory for Federals. The charter provision also may provide for amendment only by a favorable vote of 75 percent of the total votes eligible to be cast.

Management employment contracts and qualified stock option plans also may be adopted at the meeting at which the conversion plan is voted.

3. Proxy Statement. The conversion regulations contain extensive disclosure requirements for proxy statements used to obtain approval of plans of conversion. No proxy statement, form of proxy or other proxy soliciting material may be used until its use has been authorized by the Board. Disclosure includes a summary of the plan of conversion, use of proceeds from the sale of the stock, a description of the business of the converting association, information concerning the qualifications, remuneration and transactions with its directors and officers, and full audited financial statements.

4. Notice Requirements. An association considering the adoption of a plan of conversion is required to maintain this consideration on a confidential basis. Promptly after adoption of a plan of conversion by its board of directors, a converting association is required to notify its members of the action by publishing a notice in a newspaper of general circulation in each community in which it has an office, or by mailing a letter to each member. The association also may issue a press release with respect to the action. The association also is required to have a copy of its plan available for inspection by its members at each of its offices. After filing its conversion application with the Board and being ad-

vised that its application is not materially incomplete, the association is then required to publish a newspaper notice in each community with respect to the filing of its application. The notice must say that written comments from members on the plan of conversion will be considered by the board if filed within 20 business days.

5. Offering Circulars. The final offering circular for the subscription offering and the final offering circular for any public offering or private distribution of unsubscribed shares must be declared effective by the Board before its use. The offering circulars must contain substantially the same information required for the proxy statement and may be in a "wraparound" form with the proxy statement attached. The offering circulars also must provide certain additional information as to the offering. A final circular for the subscription must accompany or precede each order form for purchase of shares in the subscription offering.

6. Pricing. The proxy statement must set forth an estimated subscription price or price range. The range should normally be no more than 15 percent above and below the average of the minimum and maximum prices in the range. The Board reviews the price information in considering whether to give approval to the conversion. In this connection, the regulations provide guidelines for the independent appraisal that the converting association must file as the basis for the determination of pro forma market value.

A maximum subscription price must be stated on each order form used in the subscription offering. This price must be within the price range stated in the Board's approval of the plan of conversion. If either the maximum subscription price or the actual subscription price is not within this range, the association must obtain an amendment to the Board's approval. Before having its final offering circular declared effective by the Board, an association may be required to provide an updated appraisal.

Summing Up

Sale-of-stock conversions are a workable and desirable option for certain associations. There are sound public policy reasons for allowing this choice. Sale-of-stock conversions are proceeding under careful and extensive regulation by the Board. These regulations are sufficient to prevent windfalls to account holders, management, and investors. No association that prefers to remain a mutual is being forced to convert. Most mutual associations will continue as mutuals. There is no need for any statutory limitation on the number of conversions which the Board may approve. ■

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~~EDITOR & PUBLISHER~~

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March 7, 1978

TELEPHONE
(202) 543-1700

Julius J. Brecht, Director
~~Division of Banking & Securities~~

Poucah D
Juneau, Alaska 99811

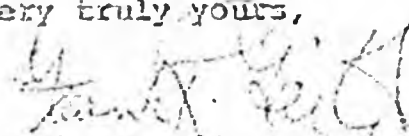
Dear Julius:

Thank you for your call today. In my capacity as General Counsel to National Association of Savings and Loan Supervisors I am pleased to respond to the report you received that stock conversions had provided a means for organized crime to acquire control of savings and loan associations.

Based upon my experience, I can state flatly that: (1) I have no knowledge of any such development occurring at any time in connection with the conversion of any institution; (2) I am certain that no such circumstance has arisen since the early 1950's when I took an active interest in this subject matter, and (3) that such a circumstance could not occur under the Federal rules and regulations now in effect respecting savings and loan stock conversions.

On the latter point, I would refer you to 5563b.3(c) of the Rules and Regulations for Insurance of Accounts issued by the Federal Savings and Loan Insurance Corporation. That regulation is captioned "required-provisions in plans of conversion". It provides, in pertinent part, as follows: "The Plan of Conversion shall...provide for an eligible record date which shall not be less than 90 days prior to the date of adoption of the plan by the converting insured institution's Board of Directors...". The import of language last quoted is that those eligible to purchase stock issued in connection with a conversion are those with funds on deposit not less than 90 days before the Board of Directors adopts the plan of conversion and as a consequence gives the first public notice of the intention of the institution to convert.

Very truly yours,


Frank R. Gallor

FRG:jh

AN ACT TO AUTHORIZE THE ADMINISTRATOR OF THE SAVINGS AND LOAN
DIVISION TO APPROVE THE CONVERSION OF A MUTUAL SAVINGS AND LOAN
ASSOCIATION TO A STOCK OWNED ASSOCIATION

The General Assembly of North Carolina enacts:

Section 1. A new §54A-4 of the General Statutes is enacted
to read as follows:

§54A-4. Conversion of a Mutual Savings and Loan Association
to a Stock Owned Savings and Loan Association. The Administrator of
the Saving and Loan Division shall promulgate rules and regulations
governing the conversion of a savings and loan association from
mutual owned to stock owned. These rules and regulations shall
include requirements that:

(1) The conversion shall neither impair the
capital of the converting association

nor diminish its ability to continue
safe and proper operations.

(2) The rights, liabilities, obligations and
relations of any person to the converting
association shall not be altered as a
result of its conversion.

(3) The conversion shall be fair and equitable
to all members and employees of the converting
association.

(4) The citizens of the communities or counties
served by the converting association and the

citizens of North Carolina in general shall not be adversely affected by the conversion.

(5) Conversion of an association shall only be accomplished pursuant to a plan approved by the Administrator. Said plan shall be

approved by the Board of Directors of the converting association and a fair and

and fair disclosure an affirmative vote of 51 percent of the total votes which members of the converting association are eligible and entitled to cast.

(6) The plan of conversion shall provide that:

a. all shares of stock issued in connection with the conversion shall be made available to the members of the converting association.

b. a uniform date shall be fixed by the Administrator for determination of the members to whom stock shall be made available.

c. stock shall be made available to members

based upon a formula approved by the

and equitable by the Administrator and

fully disclosed to the members of the converting association.

-3-

No member, officer, director, shareholder or employee

of converting association shall initially acquire

more than 10 percent of the stock made available in

connection with the conversion. ~~In business associa-~~

~~tion or group of persons acting in concert (other than~~

~~the association or board of directors) shall initially~~

acquire more than 30 percent of the stock made avail-

able in connection with the conversion.

Section 2. §54A-1 of the General Statutes is amended by striking
the last sentence.

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To: Julius J. Brecht, telecopy # 907-586-2165



National Association of
State Savings & Loan Supervisors

1001 CONNECTICUT AVENUE, N.W., SUITE 800 WASHINGTON, D.C. 20006 • (202) 452-1523

February 14, 1978

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Julius J. Brecht, Director
Division of Banking and Securities
Pouch D
Juneau, Alaska 99811

Re: Stock Savings and Loan Associations

Dear Mr. Brecht:

This is in response to a request of last Friday for the views of the National Association of State Savings and Loan Supervisors, 1/ with respect to stock savings and loan associations. The National Association of State Savings and Loan Supervisors ("NASSLS") does not as a matter of policy take positions on the desirability of legislation pending in the several states. It, therefore, neither supports nor opposes the provision of authority for stock

1/ The members of the National Association of State Savings and Loan Supervisors regulate state chartered savings and loan institutions in the several states and territories. They supervise approximately 2900 institutions having assets in excess of \$140 billion. The officers of the Association are R.J. McMahon, President of the Association and Commissioner of Savings and Loan Associations, Wisconsin; Richard J. Francis, First Vice President of the Association and Commissioner of Finance, Michigan; and Alvis J. Vandygriff, Second Vice President and Commissioner of Savings and Loans, Texas.

Julius J. Bracht
February 14, 1978
Page Two

savings and loan associations under Alaska law. As the General Counsel of NASSLS, I am, however, pleased to digest and provide materials which we have assembled on this subject. They follow.

Thirty states have stock savings and loan associations ("stock S&LAs"). In recent years, Florida, New Jersey, North Carolina, Tennessee, and Wisconsin, have authorized stock S&LA's. This year, the legislatures of not only Alaska, but also, Maryland, Alabama, Missouri, and West Virginia will consider stock S&LA legislation. In 1973, the Congress provided authority for Federal S&LA's (all of which theretofore were mutually owned) to convert to stock S&LA form of ownership. ^{2/} Pursuant to that authority 32 mutual S&LA's have, with the approval of their respective members and the Federal Home Loan Bank Board ("FHLBB") converted to stock form of ownership. At December 31, 1976, there were 732 stock S&LA's operating in the several states with aggregate assets of \$86.7 billion. On that date, stock S&LA's held 22.1 percent of the total assets of all S&LA's.

From time to time there have been charges that S&LA's of the stock form involve a higher element of risk to the safety of depositors' funds and, therefore, require more careful general supervision. We are not aware of any definitive empirical basis for these assertions. We suspect that Professor Hestor may have accurately portrayed the situation. In his report, which was released by the FHLBB in 1968, he concluded:

"... for a number of reasons, theory lends precious little insight into expected differences between stock and mutual associations. It is likely that stock associations will be more aggressive than mutuals in exploiting opportunities. It seems plausible that stock associations should be observed to grow faster and take more risks..."

^{2/} 12 U.S.C. 1725(j)(3).

Julius J. Brecht, Director
February 14, 1978
Page Three

Professors Bingham and Pettit, too, were wont to go beyond theoretical generalization in attempting to differentiate between the performance and risks of stock and mutual S&LA's:

"Key differences include the possibility of obtaining capital gains in the stock sector, differences in the way control is exercised, possible differences in retirement ages, possible differences in nepotism, differential ability to raise new capital, possible danger of undue emphasis on short run profits in the stock sector, differential ability to retain management personnel (stock options), and differential willingness and ability to merge. In our judgment none of these factors should be very important in the aggregate, but when the effects of all of them are added up the net effect should be to cause the stock sector to (1) exhibit the faster rate of growth, (2) be somewhat more profitable in the long run, (3) possibly have lower cost ratios when other factors are held constant, but (4) show up as somewhat riskier than mutuals..." "Effect of Structure on Performance in the Savings and Loan Industry", Study of the Savings and Loan Industry", prepared for the FHLBB, Vol. III, p. 1202.

The most recent empirical study of the comparative performance of stock and mutual S&LA's was prepared by Donald M. Kaplan, Director of the Office of Economic Research of the FHLBB. It found that "(S)tock chartered associations are more profitable than mutuals..."

It may be of interest to note that in those states in which State chartered associations predominate, the laws provide for stock S&LA's. California, Ohio and Texas (which respectively rank 1, 4 and 6 among the states in S&LA assets) provide for stock associations; in those states, S&LA's are the prevalent form of S&LA. This condition permits the legislatures of those states to influence the availability of mortgage credit, specifically, and consumer protection, generally, through their control of legislation affecting State S&LA's.

Julius J. Brecht, Director
February 14, 1978
Page Four

I trust this will prove helpful and hope you will feel free to call on NASSLS or me should you wish further assistance.

Very truly yours,

National Association of State
Savings and Loan Supervisors

By: Frank R. Gailor
Frank R. Gailor, Esq. *FRG*
General Counsel

cc: NASSLS Directors

FRG/aw

States which have authorized savings and loan associations
to issue negotiable order of withdrawal.

Connecticut
Maine
Massachusetts
New Hampshire
Rhode Island
Vermont
Wisconsin *

* Only state chartered associations permitted.

February 18, 1978

Mr. Joseph H. McKinnon
Pouch V
Juneau, Alaska 99811

Dear Mr. McKinnon:

We appreciate the courtesy that was extended to us last wednesday by you and the committee in regards to House Bill No. 703.

Enclosed are some suggestions in regards to this bill, which I feel are necessary for an association to operate efficiently.

If we can be of further assistance, please do not hesitate to contact us.

Sincerely,



Eddie J. Turner
1331 W. 26th. St. #10
Anchorage, Alaska 99503
Phone: #279-2962

H B No. 703

Sec. 3. AS 06.30.030 Line 27 Page 1

Delete: (banking and savings)
Substitute: savings and loan

Sec. 4. AS 06.30.035 Line 19 Page 3

The amount of the expense fund should be defined,
either by a dollar amount or percentage of capitalization.

Sec. 4 AAS 06.30.035(n) Lines 9 thru 15 Page 7

This subsection should be deleted. The appropriate
place for securities regulation is in the Alaska
Securities Act (AS 45.55).

Sec. 7 AS 06.30.060(b) Lines 1 thru 4 Page 10

^{AS}
The subscription requirements should be modified to read
as follows:

- (1) in communities having less than 25,000 inhab-
itants, the minimum sum of \$500,000;
- (2) in communities having between 25,001 and
100,000 inhabitants, the minimum sum of \$1,000,000; and
- (3) in communities having 100,001 or more inhab-
itants, the minimum sum of \$2,000,000.

Such subscription requirements coincide with the federal
requirements. See FHLBB, FSLIC Outline of Information (in
support of Application for Insurance of Accounts).

Sec. 8 AS 06.30.060(e) Line 1 Page 10

The amount of the expense fund should be defined,
either by a dollar amount or percentage of capitalization.

Sec. 52 AAS 06.30.040(b)(4) Line 29 Page 7

Should read: (4) the holding of an annual meeting of the
association and method of notification of members; however,
the time and place of it may be set by resolution of the
directors of the association.

Sec. 12 AS 06.30.105(d) Line 21 Page 13

Delete: (Any number)
Substitute: A majority

Sec. 15 AS 06.30.140 Line 1 Page 15

Delete: (If authorized by vote of the members the directors may elect all directors.)

Substitute: The Board of Directors may fill vacancies occurring on the board, such appointees to serve until the next annual meeting of the members.

Sec. 19 AS 06.30.295 Line 21 Page 17

Delete: (security)

Substitute: account

Sec. 21 AS 06.30.335(a) Line 17 Page 18

Add two sentences in the beginning.

Each association shall be operated from the home office in the state. All branch offices and agencies shall be subject to direction from the home office.

Sec. 24 AS 06.30.445(a) Lines 18 thru 27 Page 21

Delete complete paragraph.

Substitute: A savings and loan association shall establish and maintain a general reserve account for losses and other net worth accounts adequate to assure solvency of the association.

At the annual closing date following the anniversary of its certification of authority and each annual closing date thereafter, the general reserve shall have an amount fixed by regulation.

The regulation shall fix the required minimum amount of general reserve accounts of the association. The regulation shall provide a uniform schedule of minimum levels to be reached during the first 20 or more years of an association's operation for the purpose of achieving an orderly accumulation of the general reserve account.

An association may establish reserve accounts, in addition to the general reserves, as its board of directors may authorize, and make transfers to and charge such reserve accounts.

The department may permit an association to cure a deficiency in its general reserve account by requiring the board of directors of the association to earmark earned surplus, voluntarily pledged savings accounts of a mutual association, or capital surplus or stated capital of a stock association, as part of its general reserve account in the amounts needed to cure the deficiency. Amounts so earmarked shall be held for the same purpose as the general reserve to the extent the earmarked amounts are needed to maintain the required reserve account level.

Sec. 24 AS 06.30.445(c) Line 7 thru 11 Page 22

Delete sentence: (Whenever the aggregate of the general reserves, surplus and other reserve accounts, except those allocated for specific losses, exceed 12 per cent of the amount of members' savings of an association, the credits to the general reserve or surplus account as set out in (a) of this section are not required.)

Sec. 27 AS 06.30.500(1) Line 2 thru 4 Page 24

Delete: (\$75,000 on a single family dwelling or \$100,000 on a multiple family dwelling or other improved realty)
Substitute: The amount designated by FSLIC regulations on a single family dwelling, or per dwelling unit for not more than 4 families in the aggregate.

Sec. 27 AS 06.30.500 Line 27 Page 23

Delete: (unencumbered)
The referenceto "unencumbered" in this section should be deleted, in that it raises questions as to what creates an encumbrance. Assessments? Easements? Patent reservations?

Sec. 28 AS 06.30.500(a)(1) Line 26 Page 25

Delete: (\$75,000)
Substitute: the amount designated by FSLIC regulations

Sec. 44 AS 06.30.910(22) Page 119 of existing statutes

Delete: (judicial district in which the home office of an association is located;)
Substitute: "regular lending area" means the State of Alaska;

Sec. 11 AS 06.30.090 Line 21 and 24 Page 11

Delete: (of the home office)

Sec. 27 AS 06.30.500(7)(A) Line 13 Page 25

Delete: (21 years)
Substitute: 2 years beyond the maturity of the loan

Sec. 27 AS 06.30.500(7)(B) Line 15 Page 25

Delete: (70)
Substitute: 80

Sec. 6 AS 06.30.045(b)(2) Line 10 Page 9

Delete: (individual)

Memorandum

To: File No. A-4969/Peninsula Savings & Loan Assn.

From: RED

Date: February 8, 1978

Re: Recommended changes to HB703

Section 4.

AS 06.30.035(d)(1) should be revised to read as follows:

(d) The incorporators shall submit to the department

(1) An application for approval signed by all of the incorporators....

The present reference to "commencing business" is more appropriate AS 06.30.045(a), and a second reference in AS 06.30.035(d) creates ambiguity.

AS 06.30.035(d)(1)(D)(i) should delete reference to "and the amount of the expense fund," in that the amount would be then undetermined under AS 06.30.060(e).

The first sentence of AS 06.30.035(f) should read as follows: "The department shall notify the incorporators within 30 days of its decision on an application for a proposed association." Alternatively, the first sentence may be deleted, in that it is not needed in light of the remaining provisions of that subsection.

A new subparagraph (5) should be added to AS 06.30.035(g) to read in substance as follows: "That any person may file written objections to approval of the association's application within 30 days after publication of notice." Such provision will advise the public of their rights pursuant to AS 06.30.035(j).

AS 06.30.035(i)(4) shall be deleted. It is unrealistic to presume that any subscription amount, either

savings or capital, would be paid by any investor at such early stages of the formation and organization of an association.

AS 06.30.035(n) should be deleted. The subsection begins by referring to "any offering circulars," then refers to "the incorporators," and then goes on to refer to "the notice"; the section is a hodgepodge of unrelated items. No "offering circulars, prospectuses or other materials are required, see AS 45.55.140(a)(3), and any references thereto should be deleted as unnecessary. The "appropriate place" for securities regulation is in the Alaska Securities Act (AS 45.55), and any requirement for "review and approval" of offering circulars, prospectuses or other materials must await repeal of AS 45.55.140(a)(3). Likewise, there is no "notice" required to accompany any solicitation of savings or stock subscriptions, much less any "provisions of this section" which refers to any such "notice". The department already has authority to order the incorporators to cease "proceeding unlawfully," see AS 06.05.005(4); it is hard to perceive why the department may need additional powers to order the incorporators to cease "not acting in good faith." For all these reasons, AS 06.30.035(n) should be deleted.

Section 5.

AS 06.30.040 with reference to bylaws goes well beyond the usual bylaw requirements for any Alaska business corporation, see AS 10.05.135, or for a federal savings and loan association, see 12 CFR §544.5; indeed, there are no bylaw requirements for Alaska state commercial banks under AS 06.05. Accordingly, AS 06.30.040(b) should be deleted, in that many of its provisions infringe on management or board of director discretion, are subject to constant, if not daily, change, and may well concern confidential infor-

mation. However, there should be some provision added to AS 06.30.040(a) with reference to amendment of the bylaws. See AS 10.05.135.

Section 6.

The second sentence of AS 06.30.045(a) should be deleted. This is a very stiff penalty which turns on interpretation of a very vague concept of what is or is not "incidental" to commencement of business.

Reference to "savings subscriptions" should be deleted from AS 06.30.045(b)(1)(A). See comments to AS 06.30.060(h).

The reference to "individual" should be deleted from AS 06.30.045(b)(2).

Section 7.

The subscription requirements should be modified to read as follows:

"(1) in communities having less than 25,000 inhabitants, the minimum sum of \$500,000;

(2) in communities having between 25,001 and 100,000 inhabitants, the minimum sum of \$1,000,000; and

(3) in communities having 100,001 or more inhabitants, the minimum sum of \$2,000,000."

Such subscription requirements coincide with the federal requirements. See FHLBB, PSLIC Outline of Information (in support of Application for Insurance of Accounts).

Section 8.

The first sentence of AS 06.30.060(e) should be amended to read as follows: "...in an amount not less than that specified by regulations promulgated by the department." As presently written, potential incorporators have little guidance upon which they may plan, and the department is

granted too much discretion as to creation of the expense fund.

Section 9.

The first sentence of AS 06.30.060(f) should be amended to read as follows: "...may be repaid pro rata according to amounts contributed by contributors from the net earnings...."

Section 10.

AS 06.30.060(h)(2) should be deleted. An association is required to obtain Federal Savings and Loan Insurance Corporation (FSLIC) coverage prior to issuance of a certificate of authority, see AS 06.30.045(b)(4); the Federal Home Loan Bank Board (FHLBB), agent of the FSLIC, already requires savings subscriptions in the minimum amount of \$500,000. More importantly, the FHLBB allows payment of such subscriptions after the association is allowed to commence business; again, it is unrealistic to presume that any investor would deposit savings in an association prior to its receipt of a certificate of authority or prior to its "opening its doors" for business.

Section 11.

The reference to "of the home office" should be deleted in the preamble and subsection (1) of AS 06.30.090. The second reference to "of the home office" in AS 06.30.090(1) should be changed to "of the association." Further, it appears more appropriate that the secretary sign, as opposed to any "two officers," the notice of publication, see AS 06.30.090(1), and perhaps the "two officers" referred to in AS 06.30.090(2) should be specified as the president and secretary.

Section 14.

AS 06.30.115(c) should make exceptions for inspection pursuant to court orders and pursuant to the consent of the other member.

Section 16.

AS 06.30.145(c) should be deleted as an anachronism. (Perhaps the provision should be deleted in AS 06.05.435 also.)

Section 18.

AS 06.30.280(7) should be amended to read as follows: "...together with its interest in collateral securing the same."

Section 19.

The first sentence of AS 06.30.295 should be deleted, and the following sentence inserted: "Only savings accounts shall be issued, sold, negotiated, or advertised for sale either to members or to the public." I am quite concerned about the definitional problems surrounding the term "investment security" in the context of federal and state securities laws. The second sentence of AS 06.30.295 should read as follows: "...and those accounts are authorized by the Federal Savings and Loan Insurance Corporation," in that the reference to "insured" inadvertently fails to include accounts with balances in excess of \$40,000. See 12 CFR §§ 561.6, 563.3-1.

Section 24.

Reference to "mutual" should be deleted from the second sentence of AS 06.30.445(a).

Section 25.

The second and third sentences of AS 06.30.455 require dividends to be paid or declared "equally," "pro rata," "according to [certain] rate limitations," and "on the withdrawal value." It is suggested that the ambiguity created by such multitude of standards may be avoided by changing the second sentence to read: "All savings account holders shall participate in dividends not exceeding the rate limitations prescribed...."

Section 27.

The reference to "unencumbered" in the preamble of AS 06.30.500 should be deleted, in that it raises questions as to what creates an encumbrance. Assessments? Easements? Patent reservations? What is the purpose, if any, of inserting the requirement that the property be "unencumbered" as long as the association acquires a first mortgage position?

A definition of "mortgagor" as found in AS 06.30.500(1) is required in light of various family and business relationships, e.g., Mr. Jones, individually, and as majority stockholder of Jones, Inc.

Associations should be granted the authority to make construction loans; accordingly, the preamble to AS 06.30.500 should read as follows: "...an association may invest in first mortgages on real property, including leasehold estates, and including mortgages securing loans made for the purpose of construction, subject to the following limitations:"

AS 06.30.500(5) should be deleted to allow state savings and loan associations to compete with the state-wide lending powers of federal savings and loan associations. See 12 CFR §545.6-6. Further, AS 06.30.500(5) is inconsistent with the state-wide powers granted in AS 06.30.500(3).

Subparagraphs (A) and (C) of AS 06.30.500(7) could be combined in a single paragraph to the effect that the mortgage must amortize within a certain number of years prior to the end of the lease term. Paragraph (B) of such subsection should be increased from 70% to 80% for consistency with AS 06.30.500(2), .505(d), .555(b)(2).

Section 33.

A definition of "service corporation" as used in AS 06.30.616(a)(1) is required, either by statute or regulation.

Section 37.

AS 06.30.836 should be deleted. The provision is entirely too broad, giving the department power to dissolve

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an association for any reason whatsoever. It is suggested that the commissioner's powers are sufficiently broad under AS 06.05.005 to dissolve an association for good and valid reasons. An association which does not obtain a certificate of authority and commence business within one year from approval of its application would forfeit its corporate existence under present statute. See AS 06.30.095. Accordingly, AS 06.30.836 is not only not necessary, but also is subject to abuse.

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