<u>Mutual Alert</u>

Win for Mutual Institutions in Eighth Circuit Court

On August 7, 2019, the Eighth Circuit Court dismissed a Missouri case in which two mutual thrift depositors claimed they were entitled to a distribution of the their thrift's capital at the time of the merger between Inter-State Federal Savings and Loan Association (Kansas City, MO) and First Federal Bank of Kansas City (Kansas City, MO). Depositor plaintiffs of Inter-State Federal claimed the merger was inequitable because of an alleged $25 million "capital differential" between the two institutions and requested that the board of directors distribute the $25 million to depositors of Inter-State Federal. Inter-State's board of directors rejected the plaintiff's position and stated that the board would use the capital in "a manner that maximizes the benefits to all parties consistent with the overall safety and soundness of the institution". Subsequently, the depositors of Inter-State Federal filed a class action suit seeking over $5 million in damages and argued that their "ownership interest" was diminished by the merger. The defendants filed a motion to dismiss and the Missouri Bankers Association, American Bankers Association, and OCC all filed friend-of-the court briefs in support of First Federal Bank in favor of the dismissal. Following the dismissal, the plaintiffs filed an appeal.

The Eighth Circuit Court in a well-reasoned opinion ruled that the lower court properly dismissed the case, that the plaintiffs were not entitled to the surplus and there is no right to a "mandatory distribution" of retained earnings. In addition to Supreme Court precedent which explains that a mutual's surplus is "primarily a reserve against loses" and that depositors do not have substantial ownership interests in an institution's surplus, the OCC stated that any mandatory distribution would violate OCC supervisory policy which favors retention of capital particularly in the case of Federal Savings Associations because of their limited capacity to raise capital. The plaintiff's also claimed that they were entitled to a vote on the merger which was rejected by the Court as neither the Inter-State charter nor OCC regulations supported that claim.

While this case is technically limited to federal mutual institutions its holding is a resounding victory for the proposition that mutual depositor's rights are inchoate and do not equate with stockholder rights. However, the reasoning walks a fine line between the discretion of a federal mutual Board vs the governance rights of mutual federal association members. We continue to guard against misinterpretations of the diminution of rights of mutual members that would impair attempts of mutual banks to control their own independence and destiny.