Administrative Law -- Power of Federal Reserve Board to Deny Applications Under Bank Holding Company Act -- Premium Payments to Majority Shareholders -- Western Banchores, Inc. v. Board of Governors of the Federal Reserve System

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Administrative Law—Power of Federal Reserve Board to Deny Applications Under Bank Holding Company Act—Premium Payments to Majority Shareholders—Western Bancshares, Inc. v. Board of Governors of the Federal Reserve System.¹—On December 21, 1970, Jack B. Berkley, President of Stockton National Bank in Stockton, Kansas, ascertained that Mr. and Mrs. John McCormick were willing to sell their shares of Rooks County State Bank of nearby Woodston, Kansas, for $521.51 per share. At that time, the McCormicks owned seventy-seven percent, or 383½ shares, of the 500 outstanding shares of Rooks County State Bank. Jack Berkley and his family met to discuss the possibility of acquiring this stock, and at the conclusion of this meeting Jack was authorized to purchase the McCormick shares on behalf of the Berkley family. Jack's brother, Robert, an attorney, was directed to organize a bank holding corporation² in the name of Western Bancshares, Inc., which was to be the assignee of the purchased stock.

On December 23, 1970, Jack Berkley acquired the McCormick stock upon payment of $521.51 per share. On the same day, he notified the remaining shareholders of the Rooks County State Bank that he and his associates had acquired eighty-three percent of the bank's stock. Significantly, he did not disclose to them the price per share he had paid for the McCormick stock.³ He offered to purchase each of the outstanding shares at $160.00, and bought 31 shares at that price during the first week of January 1971. On January 8, 1971, Western Bancshares, Inc. was incorporated under the laws of

¹ 480 F.2d 749 (10th Cir. 1973).
² The Bank Holding Company Act Amendments of 1970 define a bank holding company as follows:

(a)(1) Except as provided in paragraph (5) of this subsection, "bank holding company" means any company which has control over any bank of [sic] over any company that is or becomes a bank holding company by virtue of this chapter.

(2) Any company has control over a bank or over any company if—

(A) the company directly or indirectly or acting through one or more other persons owns, controls, or has power to vote 25 per centum or more of any class of voting securities of the bank or company;

(B) the company controls in any manner the election of a majority of the directors or trustees of the bank or company; or

(C) the Board determines, after notice and opportunity for hearing, that the company directly or indirectly exercises a controlling influence over the management or policies of the bank or company.

(3) For the purposes of any proceeding under paragraph (2)(C) of this subsection, there is a presumption that any company which directly or indirectly owns, controls, or has power to vote less than 5 per centum of any class of voting securities of a given bank or company does not have control over that bank or company.

12 U.S.C. §§ 1841(a)(1)-(3) (1970). By the inclusion of § 1841(a) in the Bank Holding Company Act Amendments of 1970, the Act was amended to include the one-bank holding company.

³ Berkley had also acquired the stock of two other officers of the Rooks County State Bank at a price of $400 per share. As in the case of the McCormick stock, he did not disclose the amount paid for these shares to the minority shareholders. 480 F.2d at 751.
Kansas, and Jack Berkley assigned the shares of the acquired stock to the holding company.

The Bank Holding Company Act Amendments of 1970, which extended the Act's coverage to the one-bank holding company, became effective December 31, 1970. A one-bank holding company was defined by the Act to be a company which owned a controlling interest in a single bank. Western Bancshares, Inc. was such a one-bank holding company, and thus came within the ambit of the 1970 Amendments. Under section 3(a)(1) of the Act, prior approval of the Board of Governors of the Federal Reserve System (the Board) was required in any transaction "that causes any company to become a bank holding company." Pursuant to an order it had issued on June 22, 1971, the Board considered Western Bancshares' application for approval of the retention of its controlling block of the voting shares of Rooks County State Bank. The Board denied the application and ordered Western Bancshares to divest itself of all interest in the acquired bank. Two reasons were given for the Board's divestiture order: (1) the failure of the holding company to seek prior Board approval for the acquisition, and (2) the failure of the holding company to disclose to the minority shareholders of the acquired bank that their shares had been purchased for a price substantially lower than that paid for the majority interest. The Board reasoned that even though approval would have no effect upon either existing or potential competition, which were the explicit factors for Board determination set forth in section 3(c) of the Act, divestiture would be required because nondisclosure of

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8 Id. Western Bancshares, Inc. also applied for approval of retention of an insurance agency. Id.
9 Id. at 18,244. Four governors ordered divestiture, while two others dissented. Chairman Burns was absent and did not vote. Id. at 18,244 n.2.
10 480 F.2d at 750.
12 12 U.S.C. § 1842(c) (1970) provides:

The Board shall not approve—

(1) any acquisition or merger or consolidation under this section which would result in a monopoly, or which would be in furtherance of any combination or conspiracy to monopolize or to attempt to monopolize the business of banking in any part of the United States, or

(2) any other proposed acquisition or merger or consolidation under this section whose effect in any part of the country may be substantially to lessen competition, or to tend to create a monopoly, or which in any other manner would be in restraint of trade, unless it finds that the anticompetitive effects of the proposed transaction are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served.

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the disparate offers made to the shareholders would not be in the public interest.\textsuperscript{13} On appeal,\textsuperscript{14} in reversing the decision of the Board, the Court of Appeals for the Tenth Circuit HELD: the Board of Governors of the Federal Reserve System lacks statutory authority, express or implied, to deny applications for approval of formation of one-bank holding companies or of acquisition of a bank by a bank holding company solely on the basis of a finding that approval would not be in the public interest because of disparate price offers made to minority and majority shareholders for the purchase of their shares.\textsuperscript{15} The court reasoned that neither the express language nor the legislative history of the Act supported the Board's interpretation of its powers thereunder and that, had it so intended, Congress could have conferred such power upon the Board. The court noted in this regard that the statute established specific standards to guide Board action and did not authorize negative action based upon a broad determination of the public interest.\textsuperscript{16}

In deciding that a federal agency may not expand its powers beyond those expressly granted by its enabling act, the Tenth Circuit's decision in \textit{Western Bancshares} follows the substantial weight of federal precedent which refuses to allow a federal agency to expand its authority on the basis of powers not expressly or

\textsuperscript{13} Effective Sept. 1, 1971, the Federal Reserve Board promulgated certain guidelines for approval of holding company acquisitions, which guidelines included the mandate that "if any offer to acquire the shares is extended to shareholders of the bank, the offer is extended to all stockholders on an equal basis." 480 F.2d at 751 (emphasis omitted). These guidelines are found in Rules Regarding Delegation of Authority, 12 C.F.R. § 265.2(l)(22) (1973). These rules delegate power to Federal Reserve Banks to approve the acquisition of a single bank by a holding company.

\textsuperscript{14} Review of Board decisions under the Bank Holding Company Act is not a federal district court function. Review is undertaken in the appropriate United States court of appeals, but the findings of fact made by the Board, if supported by substantial evidence, are final. 12 U.S.C. § 1848 (1970).

In Whitney Nat'l Bank, 379 U.S. 411, 419 (1965), the Supreme Court held that Congress intended the statutory proceedings before the Board and the review by the courts of appeals to be the exclusive procedures in such cases.

\textsuperscript{15} The Tenth Circuit could have disposed of the case on the grounds that the acquisition of Rooks County State Bank occurred before the effective date of the 1970 Amendments to the Bank Holding Company Act. The court stated that Western Bancshares was probably a de facto corporation during December and, therefore, outside of the 1970 Amendments, which were not in effect at that time. However, the court reasoned that such a finding was not necessary to a disposition of the case. 480 F.2d at 752.

\textsuperscript{16} Id. at 753. Subsequent to the Tenth Circuit's decision, the Federal Reserve Board announced that a petition for certiorari to the United States Supreme Court had not been filed, and that the Board had determined that it would acquiesce in the \textit{Western Bancshares} decision. Wash. Fin. Rep., Oct. 22, 1973, at A-9. This decision was made apparently as a result of the Solicitor General's denial of the Board's request to seek Supreme Court review. In compliance with the decision, the Board amended its Rules Regarding Delegation of Authority (see note 13 supra) to eliminate the equivalent offer criterion from the Reserve Banks' consideration of an application. Id. at T-16 to T-17.
The decision is significant in that it deprives minority shareholders of banking institutions of the right granted under the Board’s guidelines to obtain a price for their shares equal to that received by majority shareholders in the absence of fraudulent conduct on the part of the controlling shareholders.

This note will assess the court’s decision in *Western Bancshares* and pursue the practical implications of that decision. The soundness of the Tenth Circuit’s statutory interpretation will be evaluated through an examination of the express language of the Act, the legislative history of the Act, the prior case law pertaining to interpretation of the Act, and the federal precedent dealing with the issue of construction by an agency of its enabling statute. Thereafter, the court’s decision will be analyzed to determine its effects upon the jurisdiction of the Federal Reserve Board, and upon the rights of minority shareholders to substantially equivalent price offers for their stock. A determination will be made that, as a result of the Tenth Circuit’s holding, the issue of minority shareholders’ rights to equivalent price offers must be resolved by the law of corporations of the various states. This result will be criticized on the basis of considerations of fairness and in light of the problem of shielding corporations from mismanagement of corporate assets by purchasers of controlling blocks of stock. It will be suggested that legislation be enacted that would give the Federal Reserve Board the power to better protect the rights of minority shareholders.

The Board in *Western Bancshares* contended that it was empowered under the Act and its 1970 Amendments to reject a holding company's application to acquire the shares of a bank on the grounds that the minority shares had been purchased for a lower price per share than had the majority shares. The Board argued that the words “public interest,” found in section 3(c) of the Act, the provision which specifies the factors the Board is to consider in passing upon applications for approval of bank holding company acquisitions, amounted to a “broad grant of legislative power authorizing enforcement of its guideline requiring that all stock acquisition offers must be substantially equal.” In response to these contentions, the court of appeals stated that the Board’s denial of the application was beyond its statutory powers, and that the Board’s order was “based entirely on its administrative policy requiring equal treatment to shareholders in bank acquisitions.”

The Tenth Circuit reasoned that the express statutory language of the Bank Holding Company Act did not support the construction

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19 480 F.2d at 752.
20 Id.
adopted by the Board. The relevant factors to be considered by the Board in determining whether to permit a holding company acquisition were specified in section 3(c) of the Act:

(c) The Board shall not approve—
(2) any other proposed acquisition or merger or consolidation under this section whose effect in any section of the country may be substantially to lessen competition, or to tend to create a monopoly, or which in any other manner would be in restraint or [sic] trade, unless it finds that the anticompetitive effects of the proposed transaction are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served.

The Board contended that the phrase "public interest" in this section was an implied grant of power to the Board to deny applications on the basis of public policy factors not expressly set down in section 3(c), and in this case in particular, to require equal price offers for minority shareholders' bank stock.

It would appear that the most reasonable construction of the statute would require that the Board not consider the statute's operative language, "public interest," until it had made a finding that the proposed acquisition, merger, or consolidation would have anti-competitive effects. After this finding was made, the Board would then have discretionary power to approve the application in the public interest, where it also found that the probable beneficial effects of the transaction clearly outweighed the anti-competitive effects. This interpretation of the statutory language would thus foreclose a construction authorizing the Board to base its disposition of an application solely upon an initial consideration of a broad public interest factor. It could base approval on a consideration of the public interest, subsequent to a finding that the transaction would have anti-competitive effects. There was, therefore, no explicit statutory grant of a power to deny an application which the Board found not to be in the public interest on the basis of its own independently formulated standards for approval. It would seem that had Congress intended to give the Board the authority it in fact exercised, Congress could have done so.

In addition to rejecting the Board's construction of the statutory language, the Tenth Circuit reasoned that the legislative history of the Act did not support the Board's assertion of authority. The legislative history of the Bank Holding Company Act Amendments of 1970 indicates that Congress did not intend to authorize the

21 Id.
23 480 F.2d at 752.
Board to investigate undisclosed premium payments made by holding companies in acquiring the bank stock of majority shareholders.\textsuperscript{24} In the court's opinion, the Amendments were intended to protect against future abuses committed by previously exempt one-bank holding companies in the form of the creation of monopolies, reduction of competition and extension of credit lines to finance unrelated business concerns as affiliates and subsidiaries.\textsuperscript{25} The Tenth Circuit concluded that Congress did not authorize the Board's regulation of price offerings for stock in banks by bank holding companies.\textsuperscript{26}

It is submitted that the legislative history of the Bank Holding Company Act\textsuperscript{27} supports the court's position. In 1956, Congress enacted the Bank Holding Company Act\textsuperscript{28} in order to regulate holding company activities and to regulate bank acquisitions in cases where the company controlled twenty-five percent or more of the outstanding stock of two or more banks.\textsuperscript{29} The Senate Banking and Currency Committee sought to protect the public against the dangers inherent in banking monopolies, and the Committee noted two problems which gave rise to the need for regulation: (1) the unrestricted ability of holding companies to acquire banking units and to concentrate commercial bank facilities in a particular area under a single controlling entity, and (2) the dangers posed to free competition in the banking sector by the combination of banking and nonbanking enterprises under the control of parent holding companies.\textsuperscript{30} Significantly, the legislative history did not disclose either consideration of, or an attempt by, Congress to regulate undisclosed premium payments made by bank holding companies seeking to acquire bank stock.\textsuperscript{31}

\textsuperscript{24} The phrase "premium payments" will be hereinafter used to designate that portion of the price per share paid by a purchaser to obtain a controlling interest in a corporation which is over and above the price the purchaser would have paid per share if he had not obtained control.

\textsuperscript{25} 480 F.2d at 752.

\textsuperscript{26} Id.


\textsuperscript{31} In 1966, the Bank Holding Company Act was amended to require the Board, when acting on applications for approval of acquisitions by bank holding companies, to consider the same factors that were to be considered under the amended Bank Merger Act. S. Rep. No. 1179, 89th Cong., 2d Sess. (1966), reprinted in 1966 U.S. Code Cong. & Ad. News 2393.
The legislative history of the Bank Holding Company Act Amendments of 1970 similarly indicated that Congress was not concerned with unequal price offers for stock, but rather was concerned with other problems. By 1970, twenty-three of the fifty-one banks in the United States with deposits of over one billion dollars were owned by one-bank holding companies. Six of the largest banks in the country, which held over twenty per-cent of the nation's deposits, were among the one-bank holding companies which had not been brought within the regulatory provisions of the Bank Holding Company Act prior to that time. For this reason, Board regulation of one-bank holding companies was thought to be necessary. The Chairman of the Board of Governors of the Federal Reserve System, William McChesney Martin, warned the Senate Banking and Currency Committee of the imminent risk of cartelizeing the economy, with business firms clustering about giant one-bank holding companies. It was feared that such clustering would take place for the reason that nonbanking businesses would seek to become subsidiaries of bank holding companies because of the lower interest rates and favorable credit terms that would be extended to these businesses by the bank which was controlled by the holding company. The Committee agreed that the "long-standing policy of separating banking from commerce," by prohibiting holding company ownership and control of both banking and nonbanking enterprises, should be continued. Thus, in enacting the Bank Holding Company Act Amendments of 1970, Congress intended to bring the one-bank holding company under the regulatory provisions of the Act and thereby to preserve competition in the field of banking. Nothing in the legislative history indicated that Congress intended to give the Board power to prevent disparate price offerings for bank stock by bank holding companies.

The Tenth Circuit's decision in *Western Bancshares* that the Board lacked power to regulate the price offered to stockholders for the purchase of their shares of bank stock by bank holding companies was further substantiated by the decisions of other courts.
which have interpreted section 3 of the Bank Holding Company Act. The case law under the 1956 Act disclosed that both the Board and the courts construed the Act as being designed to secure sound bank management and to preserve competition in the banking field. As the standards in the 1956 Act were substantially the same as the 1966 amended standards for Board consideration of applications for approval of bank holding company acquisitions, a review of that case law is relevant to an evaluation of the decision in Western Bancshares.

By the time of the enactment of the Bank Holding Company Act of 1956, the power of the federal government under the Constitution to create and govern banking institutions was well-established. In Continental Bank & Trust Co. v. Woodall, the Tenth Circuit, noting that a great part of this power had been delegated to the Federal Reserve Board, held that section 11(i) of the Federal Reserve Act, authorizing the Board to make rules and regulations necessary to enable it effectively to perform its statutory duties under the Act, amounted to a general grant of power to make rules and regulations which were consistent with the objective of the Act and were designed to increase the effectiveness of the Board's discharge of its duties.

Although the Board has been granted broad discretionary authority with regard to other matters within its field of expertise,

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38 See note 31 supra.
40 239 F.2d 707 (10th Cir.), cert. denied, 353 U.S. 909 (1957).
42 239 F.2d at 710. In Continental Bank, the issue arose as to whether the Board had power to conduct a hearing to determine if the bank suffered from an inadequate capital structure and should be required to surrender its stock in the Federal Reserve Bank. 12 U.S.C. §§ 1321-27 (1970) authorized the Board to require all banks to comply with the capital requirements of the Act. These sections, however, did not expressly confer power upon the Board to conduct a hearing into the adequacy of a member bank's capital structure. The court held, however, that these sections, when read as a whole and in combination with 12 U.S.C. § 248(i) (1970), which authorized the Board to establish procedures necessary to perform its duties, gave the Board the right to conduct such a hearing.
43 The Supreme Court has recently recognized the extensive discretionary authority delegated by Congress to the Board in at least one area. In an action by a magazine subscriber against a subscription service company to recover a civil penalty for failure to make disclosures required by the Truth in Lending Act, 15 U.S.C. § 1601 (1970), the Supreme Court in a divided decision, Mourning v. Family Publications Serv., Inc., 411 U.S. 356 (1973), stated that

where the empowering provision of a statute states simply that the agency may "... make such rules and regulations as may be necessary to carry out the provisions of this Act," we have held that the validity of a regulation promulgated thereunder will be sustained so long as it is "reasonably related to the purpose of the enabling legislation."

Id. at 369. In light of the legislative history of the Act, the Court found that the Board's four installment rule, requiring creditors to comply with the disclosure requirements of the Act if the sum owed is payable in more than four installments regardless of the absence of a finance charge, was reasonably related to the objective of preventing evasion of disclosure. The Court reasoned that Congress had determined to give that Act a general form and to entrust the
the powers of the Board under the Bank Holding Company Act to approve bank acquisitions by bank holding companies have been generally restricted by the courts and by the Act itself to a narrower scope.\footnote{This is the case despite the language of 12 U.S.C. § 1844(b) (1970), which confers general implementing rule-making power on the Board. The Board is given great discretionary power in the administration of § 4 of the Bank Holding Company Act, 12 U.S.C. § 1843 (1970), which deals with permissible interests in nonbanking organizations.} Under the Bank Holding Company Act of 1956, the courts have generally confined the Board's power to deny applications for approval of acquisitions by bank holding companies to situations where the Board found denial necessary for the preservation of competition and sound bank management policies. For example, in \textit{Marine Corp. v. Board of Governors of the Federal Reserve System},\footnote{325 F.2d 960, 962, 968 (7th Cir. 1963).} the Seventh Circuit reasoned that the evidence supported the Board's finding that the proposed acquisition would be detrimental to the preservation of competition in banking and, hence, that it would be contrary to the public interest. In light of this finding, the court in \textit{Marine Corp.} affirmed the Board's ruling which denied the application for approval. The Seventh Circuit did not find it necessary for the Board to consider additional factors in making its determination whether to approve the proposed acquisition.

Prior to the promulgation of the equal offer requirement in its 1971 guidelines, the Board did not contend that it was empowered under the aegis of section 3(c) of the Bank Holding Company Act to prescribe duties owed to minority shareholders. In fact, it is arguable that the Board may have initially disavowed any interest in expanding its jurisdiction into this area. In \textit{Kirsch v. Board of Governors of the Federal Reserve System},\footnote{353 F.2d 353, 356 (6th Cir. 1965).} the Sixth Circuit held that the Board had properly refused to conduct a hearing to determine whether minority shareholders claiming a breach of fiduciary duties by majority shareholders with respect to a proposed bank acquisition were entitled to relief. The petitioners were owners of minority shares in an existing holding company. They opposed the acquisition by the parent company of a certain additional bank subsidiary on the grounds that such an acquisition would be contrary to their financial interests as holders of voting trust certificates, and would also be a poor management decision. Despite these assertions, the Board granted approval of the application. In upholding the Board's decision, the Sixth Circuit indicated that the Board had not abused its discretion by declining to determine whether the majority stockholders had breached their fiduciary duties to the minority group. The court determined that the Bank...
Holding Company Act of 1956 did not require the Board to exercise jurisdiction with respect to policy differences between a corporation and its minority shareholders or minority holders of voting trust certificates when acting on an application to acquire assets of another bank. 47 In language foreshadowing the decision in Western Bancshares, the court in Kirsch stated that if the holding company, its officers, directors or voting trustees had failed to follow correct procedures or had acted unlawfully with respect to the minority owners of voting trust certificates, the issues should be resolved in the appropriate state court. 48

It is submitted that the Board in 1965, by refusing to grant the minority shareholder group a hearing, impliedly admitted that its jurisdiction over bank holding company acquisitions did not extend to a determination of whether the majority had breached a fiduciary duty owed to the minority when the majority authorized the acquisition of the subsidiary. 49 The Board's contentions in Western Bancshares represent an abrupt turnabout from its position in Kirsch. Both cases involved questions of the rights of minority shareholders which traditionally had been resolved through application of state corporation law. Furthermore, the applicable statutory language was essentially the same in both cases. The 1956 standards for approval of acquisitions, still in effect at the time of the 1965 Kirsch decision, contained the phrase "public interest" in substantially the same context as did the amended standards. 50 However, in Kirsch, the Board did not contend, as it did in Western Bancshares, that the phrase "public interest" constituted a grant of power to deny applications for approval of acquisitions by bank holding companies on the basis of a finding that the proposed acquisition would involve inequitable treatment of minority shareholders and therefore would not be in the public interest.

Although the Board declined to attempt an expansion of its powers under the Bank Holding Company Act in order to protect minority shareholders in Kirsch, it subsequently interpreted the statute as granting it extensive powers to investigate such matters as control premiums. The Board implemented its interpretation requiring equal treatment of shareholders in other bank holding company acquisitions, and in none of these pre-Western Bancshares decisions was the Board's jurisdiction to do so challenged. 51 The Board was,
in fact, commended for its efforts. The American Bankers Association, for example, voiced its approval of the Board’s requirement.\textsuperscript{52} The Federal Reserve Board in \textit{Western Bancshares} attempted to use this prior successful administrative experience under its regulation to support its arguments that it possessed jurisdiction to deny an application on the basis of unequal premium payments made to majority shareholders. Recognizing that courts, in applying the rules of statutory construction, generally give greater weight to an administrative agency’s interpretation of a statute if it is long-standing and consistent,\textsuperscript{53} the Board demonstrated that it had interpreted its enabling act to require review of undisclosed premium payments to majority shareholders, and that it had consistently applied the requirement of equivalent offers in reviewing applications for bank acquisitions. The court responded that this implementation in practice was not decisive because the Board could not exceed its statutory authority, even if its policy for doing so was sound and its implementation successful.\textsuperscript{54}

The Board might have found some support for its position in other rules of statutory construction. Courts generally give deference to an interpretation of a statute by an agency charged with the initial implementation of the statute, and, although the courts are not normally bound by such agency interpretations, it is established that such “contemporaneous constructions” should not be overruled without substantial reasons for doing so.\textsuperscript{55} The Tenth Circuit, faced with this assertion in \textit{Western Bancshares}, determined that the interpretation placed by the Board on the enabling statute could not be controlling in light of the Act’s limited grant of power to the Board. Support could be found for this position in \textit{First National Bank v. First Bank Stock Corp.},\textsuperscript{56} where, in the course of its opinion, the court stated that the interpretation of the Bank Holding Company Act by the Board of Governors of the Federal Reserve System, which administered the Act and which played an active part in its enactment, was entitled to substantial weight, but that it was not controlling.\textsuperscript{57}

The courts generally accord controlling weight to the agency interpretation where a contemporaneous construction of a statute by an agency charged with its administration finds support in the statutory language and legislative history.\textsuperscript{58} In contrast to such

\textsuperscript{52} 480 F.2d at 752.
\textsuperscript{54} 480 F.2d at 752.
\textsuperscript{56} 306 F.2d 937 (9th Cir. 1962).
\textsuperscript{57} Id. at 941.
expressly or impliedly authorized agency constructions and regulations, the rule promulgated by the Board in *Western Bancshares* amounted to an attempt to go beyond effectuation of the legislative intent. The Board's regulation added a new requirement under the Bank Holding Company Act for which no express or implied basis could be found in the Act or in its legislative history. In light of this fact, the Tenth Circuit was constrained to reject the Board's construction of its enabling Act.

It is established that administrative regulations, to be valid, must be within the confines of the powers granted to the agency by the enabling statute. In recent cases, the federal courts have not hesitated to hold administrative agency rules invalid where the rules conflict with the enabling statute and the agency, in promulgating the rules, has exceeded its statutory authority. A reviewing federal court is statutorily authorized to determine whether an administrative agency's action has exceeded its statutory bounds. The Administrative Procedure Act provides that "the reviewing court shall . . . hold unlawful and set aside agency action . . . found to be . . . in excess of statutory jurisdiction, authority, or limitations, or short of statutory right."

On the basis of these requirements the Tenth Circuit refused to uphold the equivalent offer policy promulgated by the Board under the Bank Holding Company Act.

Within the framework of the express language of the Bank Holding Company Act, its legislative history and the pertinent prior case law, it is submitted that the decision in *Western Bancshares* is correct. The Tenth Circuit properly found that the Board had been given neither express nor implied statutory authority to regulate the price which bank holding companies offered for the purchase of stock in banks, unless the Board first found that the transaction would have anti-competitive effects.

Beyond the issue of the soundness of the Tenth Circuit's statutory interpretation of the Bank Holding Company Act in *Western Bancshares*, there arise significant questions concerning the possible

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59 The term "rule" is defined in the Administrative Procedure Act as follows:

(4) "Rule" means the whole or a part of an agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy or describing the organization, procedure, or practice requirements of an agency . . . .


63 The decision in *Western Bancshares*, curtailing the asserted authority of a powerful federal agency, is not without precedent. See, e.g., cases cited in note 61 supra. The Supreme Court has determined that the powers exercised by federal agencies are limited to those authorized by the agency's enabling legislation. See NLRB v. Boeing Co., 412 U.S. 67 (1973); United States v. Chicago, Mil., St. P. & Pac. R.R., 282 U.S. 311 (1931).
implications of the *Western Bancshares* decision. One such issue involves the question of the effects the decision will have upon the Federal Reserve Board in the context of the federal bank regulatory structure. In order to analyze this issue properly, it is necessary to outline briefly this structure. There are three federal bank supervisory agencies: the Comptroller of the Currency, the Federal Reserve Board and the Federal Deposit Insurance Corporation (FDIC). The overlapping authority of these agencies in the administration of laws in some areas has "given rise to interpretative, regulatory, and policy differences, particularly in recent years." There are also indications that each of the agencies has attempted to increase its powers under the various statutes it administers, thereby giving rise to additional conflicts. Thus, within the federal bank regulatory system there apparently exists a potential for competition between agencies seeking to attain a dominant position.

The Federal Reserve Board has been given exclusive jurisdiction to administer the Bank Holding Company Act Amendments of 1970. Within the framework of the federal regulatory system of banks, such a grant of exclusive jurisdiction is unusual. Congress rejected proposals to divide administration of the Act among the three federal bank supervisory agencies. Congress thus placed the

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64 Since only a very small proportion of the banks in the nation are noninsured non-member banks, which are exclusively under state regulation, the federal bank supervisory structure determines the basic nature of bank regulation. Hackley, Our Baffling Banking System, 52 Va. L. Rev. 565, 566 (1966).

65 See Hackley, supra note 64, for a thorough discussion of the results of the overlapping powers of the three supervisory agencies.

66 See Arnold Tours v. Camp, 472 F.2d 427, 438 (1972); Wash. Fin. Rep., May 29, 1972, at T-6 to T-8; Wash. Fin. Rep., July 24, 1972, at A-1. These problems have led to several different proposals in the 1960's for the consolidation of bank regulatory power. See Hackley, supra note 64, at 802-12.

67 The Attorney General can institute an antitrust action during the first thirty days after the approval of a bank holding company acquisition by the Board. 12 U.S.C. § 1849(b) (1970).


There is some evidence that the Board has not limited its attempts to expand its powers beyond those granted to it under the Bank Holding Company Act exclusively to the matter of stock acquisition prices. The Board has been active in applying its capital adequacy requirement, despite the fact that the matter of capital adequacy has traditionally been "regarded as within the province of the particular bank's primary supervisor, Federal or State." Id. The effect of such activity by the Board is not limited to an area in which the Board possesses exclusive jurisdiction, as is the case in *Western Bancshares*, but constitutes an impingement upon the jurisdictions of other bank regulatory agencies, both state and federal. For an example of the application of the capital adequacy test by the Board, see Chicago City Bancorporation, Inc., 38 Fed. Reg. 7363 (1973). The Board has also denied an application for approval of an acquisition because of excessive management consulting fees. Valley Agency Co., 37 Fed. Reg. 22,914 (1972). It is arguable that these actions may be within the Board's power under § 3(c) of the Act, requiring the Board to consider "the financial and managerial resources and future prospects" of the banks and holding companies concerned. 12 U.S.C. § 1842(c) (1970). However, if the Board has overstepped its statutory bounds in these areas, *Western Bancshares* indicates that it will not be allowed to continue to do so.

In response to complaints by the Independent Bankers Association of America to the effect that the capital adequacy guidelines, which restricted the amount which a bank holding
Board in a potentially dominant position with respect to the other two agencies in the area of federal banking regulation. The decision of the Tenth Circuit, however, restricted the Board's powers under the Act to those expressly granted by the legislation. In this respect, it is submitted that the case could have the salutary effect of limiting some of the jurisdictional conflict among federal bank supervisory agencies by refusing to allow each agency to extend its powers beyond those given to it by Congress. However, *Western Bancshares* will probably not result in a change of the Board's status within the regulatory structure. Because the decision curtails the exercise of a power by the Board not exercised by the other agencies—the regulation of price offers in bank stock acquisitions—the Comptroller and the FDIC will not be able to enter into the vacuum created by the Tenth Circuit's decision and absorb the power to regulate such price offers. 69

It should be noted, however, that the Bank Holding Company Act itself may have the potential for establishing the predominance of the Board within the bank supervisory structure. It would not appear that the *Western Bancshares* decision has measurably limited this potential. There has been a rapid increase of both the size and the number of bank holding companies in recent years. At the end of 1970, there were 121 regulated bank holding companies with sixteen percent of the nation's deposits, whereas, at the beginning of 1973, there were 1,600 regulated bank holding companies with over sixty percent of all commercial bank deposits. 70 This growth has occurred because the Act appears to make holding company expansion more

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69 A more serious threat to the Board's power is posed by the definite trend in recent years of withdrawal of banks from Federal Reserve membership. This trend threatens to weaken the position of the Board within the federal regulatory structure. Between 1956 and 1972, 756 member banks withdrew from the Federal Reserve System. Letter from D. L. Rogers, Executive Director of the Association of Registered Bank Holding Companies, to the Board of Governors of the Federal Reserve System, Feb. 7, 1973, printed in Wash. Fin. Rep., Feb. 12, 1973, at T-3 to T-4.

The Board, however, has indicated that it may ask Congress for an amendment of its enabling act, which would require that subsidiary banks of bank holding companies become members of the Federal Reserve System, in order to limit this process of bank withdrawal and to further consolidate its power. *Hamilton Bancshares*, 38 Fed. Reg. 1307 (1973). Such a requirement would probably be enacted by Congress if needed by the Board in the administration of the monetary system, and the requirement of membership would undoubtedly establish the Board's preeminence in the bank supervisory system if superimposed upon the widespread trend of adoption of the bank holding company form of organization. In contrast to its position in *Western Bancshares*, the Board in *Hamilton* recognized the necessity of seeking a grant of power from Congress in order to increase its authority through the Bank Holding Company Act.

70 Shay, supra note 68, at T-8.
advantageous than branching in many situations, and section 4(c), permitting bank holding companies to engage in certain non-banking activities which the Board finds to be "closely related to banking," is likely to attract larger banks desiring to diversify their activities by utilization of the holding company form.

The Western Bancshares decision raises the further question as to what rights minority bank shareholders now have to obtain price offers for their stock substantially equivalent to those offered to majority shareholders. The Tenth Circuit decision indicates that the Board will have to obtain an amendment to the Bank Holding Company Act if it desires to impose the requirement of equivalent offers. Unless and until the Board procures such legislation, minority shareholders will be left to seek means of enforcing such a right in state corporation law, and, possibly in the securities laws. Although stating that it had "no argument with the Board's policy determination," the Tenth Circuit terminated the special federal protection provided by the Board to minority shareholders in banks acquired by holding companies. The Board argued for its policy requirement on the grounds that: (1) consideration of equity demanded it; (2) without it, minority shareholders would not be as willing to invest in bank stock; and (3) the requirement protected the minority from mismanagement. The Board had urged that minority shareholders needed such protection because

(1) inherent fairness justifies a policy that all shareholders be treated on an equivalent basis;
(2) to the extent that minority shareholders were treated less equitably than majority shareholders, capital financing for bank stock would be hindered; and
(3) without an opportunity to sell out on a substantively equivalent basis to majority stockholders, the minority interest in a bank suffered a precarious existence.

As will be explained below, the first and third contentions find support in the legal commentaries on this subject.

The issue of whether minority shareholders have a right to obtain price offers for the purchase of their shares equal to those obtained by the majority and controlling stockholders, or, as an alternative, have a right to share the profits derived from the sale of

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71 In First Nat'l Bank v. Camp, 465 F.2d 586, 596-97 (D.C.Cir.), cert. denied, 409 U.S. 1124 (1972), the court held that the Comptroller cannot approve branching where the state statute disallows it. The interpretation of the statute by the state authorities is not binding upon the Comptroller. State banking law restrictions upon branch banking are not applicable to bank holding companies.


73 480 F.2d at 752.

74 Id. at 752-53.

75 See text at notes 97-101 infra.
the control block, has generated a great deal of litigation and discussion. The commentators have generally agreed that minority shareholders should be accorded these rights. The case law in the majority of jurisdictions denies the existence of such rights.

It is important to note, for example, that the minority shareholders in *Western Bancshares* would not have a remedy under the law of Kansas, the state of the bank's incorporation. In *McDaniel v. Painter*, the Tenth Circuit applied Kansas law and rendered a decision representative of the majority view regarding nonequivalent stock purchases. Minority shareholders in a Kansas bank filed suit against majority shareholders for alleged breaches of fiduciary duties in the sale of the bank stock insofar as the majority failed to inform minority stockholders of the offer to purchase, and insofar as they sold the stock as insiders at a price not available to the minority. The court held that a dominant or majority stockholder did not become a fiduciary for other shareholders by reason of mere ownership of stock, and that dominant shareholders were entitled to receive a premium for their stock which reflected the control potential of the stock.

The case law in a majority of jurisdictions was summarized by the Sixth Circuit in *Seagrave Corp. v. Mount*. The court stated that there are recognized exceptions to the general rule that controlling and majority stockholders may dispose of their shares at any time and for any price they desire without incurring liability to other stockholders. Liability arises where fraud is involved in the actions of the dominant directors and stockholders, where controlling stockholders turn over their shares to purchasers who mismanage the corporation or loot the corporate assets, where non-controlling stockholders are induced to sell their shares by concealment of the fact that a premium is being paid to the controlling stockholders, where controlling stockholders or directors make a secret profit from a transaction, or where directors are dealing directly with the corporation to their own personal advantage, known or unknown.

Thus, minority shareholders' rights to profits resulting from pre-

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77 418 F.2d 545 (10th Cir. 1969). Since the Rooks County State Bank is located in Kansas, this case would be relevant precedent in an action by the minority shareholders seeking to recover their share of an undisclosed premium payment.

78 Id. at 547.

79 212 F.2d 389 (6th Cir. 1954).

80 Id. at 395.
mium payments depend upon a showing of some affirmative fraudulent conduct on the part of the majority or controlling stockholders. Mere nondisclosure of premium payments, as in Western Bancshares, would not entitle minority shareholders to share the profits. In the ordinary sale situation, therefore, the law of most jurisdictions offers little assistance to the minority shareholder. There is a minority position to the contrary. The leading case recognizing a right in minority shareholders to obtain prices equivalent to those obtained by the majority for the sale of their stock is Perlman v. Feldmann. The principal defendant, when he was dominant stockholder, chairman of the board of directors and president of the steel company in which the plaintiffs were minority shareholders, sold his stock at a premium. The plaintiffs contended that the sale of the controlling stock amounted to the transfer of a corporate asset in the form of the power to allocate the corporate product at the time it was in short supply as a result of war demand. The court reasoned that the transaction involved a sale of goodwill and the sale of the corporation's opportunity to receive interest-free loans from customers for plant modernization, and held that both directors and dominant stockholders stand in a fiduciary relationship to the corporation and to the minority stockholders. It must be noted, however, that the court limited its holding, stating that it did not suggest that a majority stockholder would never be free to sell his stock without incurring liability for profits. Thus, even the Perlman decision may be of limited value for minority shareholders.

An apt statement of the minority rule and of its rationale is found in Jones v. H.F. Ahmanson & Co., 1 Cal. 3d 93, 460 P.2d 464, 81 Cal. Rptr. 592 (1969).

The traditional judicial position was that a controlling shareholder was not a fiduciary and owed no duty to minority shareholders when he sold his stock to outsiders. See, e.g., Keely v. Black, 91 N.J. Eq. 520, 111 A. 22 (1920). Among the earliest cases to adopt a rule entitling minority shareholders to recover a pro rata distribution of the profits resulting from a premium payment was Dunnett v. Arne, 71 F.2d 912 (10th Cir. 1934). In that case, the majority stockholders-directors actively induced the minority shareholders to accept a lower price for their stock by concealing the price received for the majority stock. The court reasoned that the sale involved amounted to a corporate transaction and, therefore, imposed liability on the defendant majority shareholders for the breach of fiduciary duties owed to the majority group. Id. at 920. The limitations of this decision became apparent shortly thereafter when the Tenth Circuit held in the companion case of Roby v. Dunnett, 88 F.2d 68 (10th Cir. 1937), that, as long as he does not dominate, interfere with or mislead other stockholders, the majority shareholder is free to dispose of his stock. Id. at 69.

Perlman might be interpreted to be limited to its particular facts. The court in limiting its holding stated:

[W]hen the sale necessarily results in a sacrifice of this element of corporate good will and consequent unusual profit to the fiduciary who had caused the sacrifice he
As in the majority of jurisdictions under state corporation law, minority shareholders appear to have no right to recover under federal securities law for the sale of a controlling block of stock at a premium. Claims have been based on alleged violations of section 10(b) of the Securities Exchange Act and its implementing regulation, SEC Rule 10b-5. These general anti-fraud provisions apply to the sale in interstate commerce of any security, including bank securities not required to be registered under the Securities Exchange Act. Unlike the registration provisions of the Securities Exchange Act, which are administered by the three bank regulatory agencies with respect to bank securities, section 10(b) and Rule 10b-5 are administered and enforced by the Securities Exchange Commission. These anti-fraud provisions are intended to cover "misleading or deceptive activities, whether or not they are precisely and technically sufficient to sustain a common law action for fraud and deceit." It has been judicially established that an implied private right of action exists under section 10(b) and Rule 10b-5. Nevertheless, minority shareholders have not succeeded in recovering for damages allegedly incurred where majority stockholders should account for his gains. So in a time of market shortage, where a call on a corporation's product commands an unusually large premium, in one form or another, we think it sound law that a fiduciary may not appropriate to himself the value of this premium.

219 F.2d at 178.

Recent federal cases have suggested another possible approach to the situation where the dominant shareholders receiving the premium payment hold no position of management and, therefore, have none of the fiduciary responsibilities of corporate officers. These are the cases containing claims based on § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (1970), and on SEC Rule 10b(5), 17 C.F.R. § 240.10b-5 (1973). In Ferraioli v. Cantor, 281 F. Supp. 354 (S.D.N.Y. 1967), the court stated that the question of whether a controlling stockholder may invite some shareholders but not others to participate in the sale of controlling stock at a premium is analogous to the issue of whether trading by an insider on the basis of material undisclosed information may violate § 10(b) and Rule 10b(5). Id. at 357-58. But the court in Ferraioli did not find it necessary to reach the question of whether a controlling stockholder would violate § 10(b) and Rule 10b(5) when he sold his control stock at a premium without notifying any other stockholders. Id. at 357. However, in Christophides v. Porco, 289 F. Supp. 403 (S.D.N.Y. 1968), the same court held that the majority or dominant shareholder is entitled to receive a premium representing the control potential, and the court sharply criticized the Rule 10b(5) approach as "esoteric and implausible." Id. at 406.

In Haberman v. Murchison, 468 F.2d 1305 (2d Cir. 1972), the appellant relied on Ferraioli. The court stated that "[t]he opinion in that case cited no authority for this proposition . . . ." and went on to say that "[p]erhaps under some circumstances, the purchase of shares by one individual from another who has withheld from the seller information that the buyer has been offered a greater price for the same shares might be a deceptive practice within the meaning of Section 10(b)." Id. at 1312-13. The court subscribed to the general rule of Christophides: there is no obligation to "share and share alike." Id. at 1313.

The banking agencies have authority to administer certain provisions of the Securities Exchange Act: 15 U.S.C. §§ 78m, n(a), n(c), n(d), n(f) and p(l). 15 U.S.C. § 78l(i) (1970).
Herpich v. Wallace, 430 F.2d 792, 802 (5th Cir. 1970).

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failed to disclose that they were selling their controlling block of corporate stock in return for a control premium.

The utility of the anti-fraud provisions for minority shareholders seeking to recover for a sale of controlling stock at a premium is limited in several ways. As compared with the Federal Reserve Board's equivalent offers requirement, the claimant asserting a Rule 10b-5 claim must have been either the purchaser or seller of the securities, or he must be able to show damages flowing directly from the unlawful act of the purchaser or seller.91 Thus, the minority shareholder would have to have sold his shares at the disadvantageous price before he would have standing under Rule 10b-5, unless the court would accept the argument that the sale of the controlling stock at a premium caused damage to the minority stockholder by depriving him of a profit rightly his. As has been noted previously, courts are reluctant to accept this theory. There are indications, however, that judicial interpretations of Rule 10b-5 are becoming more liberal in allowing aggrieved individuals recourse under the rule. It has been suggested that the Supreme Court's decision in Superintendent of Insurance v. Bankers Life & Casualty Co.92 relaxed the requirement of fraud in connection with a securities transaction, so that only an indirect connection between the Rule 10b-5 fraud and the sale of securities is required.93 Thus, the minority shareholder would not have to sell to the majority shareholder, so long as the controlling shareholder's failure to disclose the premium payment received in the sale of his securities caused damage to the minority shareholder. In Affiliated Ute Citizens v. United States,94 the Supreme Court held that failure to disclose material facts, i.e., those facts which an investor might have considered important in making the decision to buy or sell, constituted a Rule 10b-5 fraud.

Assuming that minority shareholders should have the right to an equal offer, as will be discussed below, Rule 10b-5 remains inadequate, despite these two recent Supreme Court decisions, in comparison with the Federal Reserve Board's equivalent offers requirement, as a means of enforcing a minority shareholder's right to an equal price for the sale of his stock.95 At the present time, there is very little likelihood that a minority shareholder will be able to successfully assert a claim under Rule 10b-5 that the controlling stockholder failed to disclose the fact that he had received an offer for his controlling block of corporate shares which was higher than that offered minority shareholders. Even if the federal courts were

91 Erling, 429 F.2d at 799.
92 404 U.S. 6 (1971). In Bankers Life, the Court found that the "in connection with" requirement was satisfied since the corporation was injured "as a result of deceptive practices touching its sale of securities as an investor." Id. at 12-13.
93 See Note, 50 Texas L. Rev. 1273, 1286 (1972).
95 Cases subsequent to Bankers Life and Affiliated Ute indicate that the extent of liberalization by the courts may not be as great as it would first have appeared to be. See Haberman v. Murchison, 468 F.2d 1305 (1972), discussed in note 85 supra.
to find that a majority shareholder had a duty to disclose such an offer, the protection afforded minority bank shareholders under Rule 10b-5 would still fall short of that provided by the Federal Reserve Board prior to the decision in Western Bancshares. The Second Circuit has recently held that a full and fair disclosure of all material facts is all that is required by Rule 10b-5, even where the underlying transaction may be unfair or involve a breach of fiduciary duties. According to this holding, if a controlling shareholder disclosed to the minority shareholders that he was about to receive a premium for the sale of his stock, the minority would not be able to obtain either damages or an injunction under Rule 10b-5. In order to have standing, they would probably first have to sell their shares at a disadvantageous price. Thus, under Rule 10b-5 an aggrieved shareholder could receive relief, if at all, only after the sale of the corporate stock had taken place. In contrast to this position, the Board's requirement that equivalent offers must be made to all stockholders would afford minority shareholders greater protection because it would operate before the sale of the corporate stock could be completed, as compliance with the requirement would be a prerequisite to approval of the acquisition of a bank by a holding company. Furthermore, such relief could be granted by the Board regardless of whether disclosure had been made of the higher offer.

The question as to whether new protections should be afforded minority shareholders or whether existing protections are adequate requires an initial determination that minority shareholders should have such rights. The issue of whether minority shareholders should have the right to obtain price offers for their shares equal to those obtained by majority and controlling shareholders has evoked considerable discussion among legal commentators. The adoption of a rule that all shareholders have a right to an equal opportunity to participate in a sale of stock pursuant to an offer to purchase the control block at a premium has been urged with persuasive force by Professor William D. Andrews. Professor Andrews argued that the procedure for implementing a rule whereby minority shareholders would be given an equal opportunity to participate in the sale of corporate stock was already established with respect to tender offers; the purchaser would make a tender offer, specifying the price and the number of shares, and inviting all shareholders to tender their stock if they wish to sell at that price. If more than the desired percentage of outstanding shares are tendered, the purchaser would buy pro rata from each tendering shareholder.

The arguments for and against Andrew's rule of equal oppor-

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97 See note 76 supra.
98 Andrews, supra note 76.
99 Id. at 516.
100 Id.
tunity center around questions of equity, prevention of mismanagement and effects upon investment activities. The most compelling reason for adopting the rule of equal opportunity would be that it would produce the same result as a merger or a sale of corporate assets—equality of participation in the proceeds.\(^{101}\) It may be contended, however, that implementation of the rule might have inequitable effects upon controlling shareholders in that it would reduce the value of a controlling block of corporate stock, because the shares could not be resold as a block unless either the purchaser desired to buy one hundred percent of the outstanding shares or the other shareholders failed to tender a number of shares sufficient to fulfill the terms of the offer. It is submitted, however, that the possible detrimental effects upon majority shareholders may not be extensive and in any case should not be controlling. It has been suggested that the controlling shareholder receives an adequate return for the premium which he has previously paid to obtain control through the extra protection afforded his investment by virtue of the control he may exercise during the length of his investment.\(^{102}\) Furthermore, the rule would prevent minority shareholders from being deprived of an equal right to participate in the profits derived from each share of corporate stock, a right which obtains because of the equal participation in the risk of the venture represented by each outstanding corporate share.\(^{103}\)

A second factor argues for the adoption of a rule which would provide minority shareholders with a right to obtain substantially equivalent price offers for their stock. Mismanagement by purchasers of control blocks would probably be discouraged by the rule of equal opportunity.\(^{104}\) Present state corporation law which renders directors or majority shareholders liable for negligence in the sale of their controlling shares affords their minority shareholders some protection in this respect.\(^{105}\) Under the equal opportunity rule, controlling shareholders would be unwilling to sell to purchasers suspected of planning to loot or mismanage the corporation, for the controlling shareholder would retain an interest in the corporation, unless the purchaser bought all the shares outstanding.\(^{106}\) The purchaser would have no incentive to loot the corporation if he had purchased one hundred percent of its stock, for he would then be looting his own assets.\(^{107}\) Mismanagement is a recurrent problem, and it would be especially desirable to prevent it in the banking area where the public would either pay directly, through loss of deposits,
or indirectly, through the payment by the federal government of
deposit insurance to aggrieved depositors for the consequences of
such mismanagement.

The rule of equal opportunity would, as the Board argued in
Western Bancshares with respect to the similar requirement of equi-
valent offers, serve the interests of equity and the sheltering of
minority shareholders from corporate mismanagement. Furthermore,
the rule would not prevent a purchaser from offering more
per share to acquire a controlling interest than where he does not
acquire such an interest, for, like the Board requirement that equal
offers be made to all shareholders, the rule of equal opportunity
would require only that all shareholders be extended the offer to sell
at a premium. However, purchasers, in order to reduce their
costs of purchasing a controlling interest, could buy first from minor-
ity shareholders at a lower price per share, as long as there was a
concurrent disclosure that they planned to pay more for majority
shares.109

Either the Federal Reserve Board's equivalent offer rule or
Professor Andrew's equal opportunity doctrine might have undesir-
able effects upon investment activity. The equivalent offer or equal
opportunity rules would "impose higher capital requirements on
beneficial purchasers in a substantial number of transactions" by
forcing them to buy more shares than they would have otherwise
desired.110 Sellers of control blocks would often want to sell all of
their stock, either to obtain needed cash or to avoid possible policy
clashes and the risks attendant upon loss of control. The
purchaser's investment would be more expensive under the rule of
equal opportunity, as a consequence of the costs of dealing with
additional shareholders. It is submitted that implementation of
the rule, which would be similar to the policy applied by the Board
in Western Bancshares, might discourage investment in two other
ways. The rule would have the effect of reducing the resale value of
a control block of stock in most circumstances. Institutional inves-
tors, often the owners of control blocks, take little interest in the
management powers stemming from control, and they purchase
shares primarily for investment profits. They would be discouraged
by having to pay higher prices to minority shareholders when pur-
chasing a control block under the rule. In theory, the rule could
result in deterring investment by potential controlling stockholders.

Despite the possible adverse consequences of the doctrine of
equal opportunity, it is submitted that the arguments in favor of
empowering the Federal Reserve Board to implement a regulation

108 Id. at 527.
109 Id. at 558.
110 Javaras, supra note 76, at 426.
111 Id. at 425-26.
112 Andrews, supra note 76, at 526.
similar to the equal opportunity doctrine, when passing upon applications for acquisitions of banks by holding companies, should be determinative. Considerations of equity support the adoption of such a rule: minority shareholders should have a right to share proportionately in the profits resulting from an increase in the investment value of their company's stock. A requirement of equivalent offers would tend to prevent majority shareholders from selling to purchasers who might mismanage the bank, and thereby injure a large number of depositors. In addition, in response to the position that adoption of such a rule would deter large investors from investing in bank stocks, it should be noted that the Federal Reserve Board's equivalent offer rule was in effect for nearly two years, and during that period investment in bank holding companies greatly increased.113 Furthermore, imposition of the requirement that equivalent price offers be made for the purchase of both minority and majority bank shareholders' stock would very likely be an additional incentive to the small investor to purchase shares in banking institutions.114 This result would be particularly desirable during the present period of high interest rates.

As previously stated, however, present law does not provide minority shareholders with adequate recourse to the courts in cases of undisclosed premium payments. In the great majority of states, the corporation law does not recognize any right of the minority shareholder to share in the premium received from a sale of a control block of stock. At this time, the anti-fraud provisions of the federal securities laws provide little protection to minority shareholders in this situation. Furthermore, in many instances holding companies could acquire the stock of in-state banks without using the mails, interstate commerce or the facilities of a national securities exchange, and thereby remain outside the jurisdiction of section 10(b) and Rule 10b-5.

Thus, it would appear that given the existing state of the law, the interests of minority shareholders in participating in the profits to be derived from the sale of a controlling majority of corporate stock could be best furthered by a requirement similar to the Federal Reserve Board's provision struck down in Western Bancshares. While it might be argued that the right of minority shareholders in this regard should be governed by state corporation law, it is submitted that there exists a substantial federal interest in the supervision of the nation's financial institutions. Extensive control over a

113 See text at note 70 supra. Furthermore, minority shareholder's rights under 15 U.S.C. § 78n(d) (1970) to equal participation in the proceeds resulting from mergers or sales of corporate assets and liquidation do not appear to have deterred large investors.

114 The Federal Reserve Board recognized this incentive effect when it argued that the refusal of the Tenth Circuit to uphold its regulation in Western Bancshares would have the consequence of inhibiting capital contributions in the banking industry on the part of small investors. 480 F.2d at 752.
substantial portion of the country’s banking sector has existed since the mid-nineteenth century. It would appear that federal supervision of premium payments made to majority shareholders would not be outside the ambit of this established federal interest. Furthermore, minority shareholders were given a federal right to equal participation in the proceeds deriving from tender offers under the Williams Bill, enacted in amendments to the Securities Exchange Act. Under those amendments a purchaser who has made a tender offer for shares required to be registered under the Securities Exchange Act must take up the shares pro rata during the first ten days, and must supply certain information to the appropriate regulatory agency. Thus, since the minority shareholders are informed of the impending tender offer, and since the buyer must purchase the shares offered to him during the ten-day period, whether by majority or minority shareholders, the minority shareholders are afforded the opportunity to participate in the profits to be derived from the tender offer.

In the case of registered bank stock, the provisions of the tender offer legislation are administered by the bank regulatory agency which has similar authority over its class of banks under sections 12, 14 and 16 of the Securities Exchange Act, with the exception of the general anti-fraud provision, which is enforced by the Securities Exchange Commission. For the benefit of the selling securityholders, such information as the identity of the offeror, the terms of the offer, the offeror’s source of financing (in the case of a cash tender offer), complete financial data on both the offeror and the target company (the company whose shares are solicited), and the offeror’s purposes and plans for the target company must be provided to the appropriate agency in advance of the offer. Acquisitions resulting in the beneficial ownership of more than five percent of any class of securities are within the coverage of the statute, with the exception of acquisitions during a twelve-month period which would not exceed two percent of the class. The seller may withdraw his securities during the first seven days of the offer. Congress enacted the Williams Bill despite recognition that: (1) it might deter tender offers by those reluctant to disclose the required infor-

117 Originally the tender offer legislation applied where the transaction resulted in ten percent ownership, but the statute was amended to cover transactions resulting in only five percent beneficial ownership. 15 U.S.C. § 78n(d) (1970), amending 15 U.S.C. § 78n(d) (1968).
118 15 U.S.C. §§ 78(b), (g)(1) (1970) requires registration of securities listed on a national exchange and of securities of companies with assets of over $1,000,000 and at least 500 shareholders.
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mation; (2) compliance with the regulatory process would involve additional costs; and (3) forced disclosure of the specified information might raise the price the offeror would have to pay to attract shares.\textsuperscript{123} The provisions of the federal tender offer legislation would not, however, apply in factual situations such as that in \textit{Western Bancshares}. The reason for this is that the tender offer does not by definition encompass a nonpublic offer to purchase securities from a small number of large shareholders,\textsuperscript{124} which presents the typical situation in which controlling blocks of stock are sold for a control premium. Thus protection for minority shareholders must be provided by other federal legislation.

The implementation by the Federal Reserve Board of its policy that stock purchase offers must be extended to all shareholders of the same class on an equal basis amounted to a requirement that a tender offer be made. The nonpublic sale of control remains the only method of transferring control whereby the dominant shareholder is able to profit disproportionately to the detriment of minority shareholders. The Board should be allowed to impose the requirement that holding companies seeking to acquire control of banks extend equal offers to all shareholders. As a result of the decision in \textit{Western Bancshares}, this can only be accomplished through legislation. It is submitted that the information required to be disclosed to the appropriate agency for public inspection under the federal tender offer legislation should also be required to be disclosed by holding companies seeking to acquire control of banks for the protection of the banks' shareholders. The disclosure of such information would lead to informed decision-making, which is a major objective of federal securities law. Furthermore, the provisions of the amendments to the Securities Exchange Act requiring that shares be taken up pro rata during the first ten days only and that the seller may withdraw his shares during the first seven days should also be included in the legislation, as they appear to be reasonable and workable. Administration of such legislation should be exclusively vested in the Board in the case of bank holding companies. Responsibility should not be divided between the three banking agencies and the Securities Exchange Commission. Such a division of authority would create administrative waste and inefficiency, as the Board is presently required to process applications for the acquisition of banks by holding companies.

On the basis of the express statutory language of the 1970 Amendments to the Bank Holding Company Act and the rules of statutory interpretation, the Tenth Circuit's decision in \textit{Western Bancshares} appears correct. As a consequence of that decision, however, the Board will not be allowed to expand its authority under the Bank Holding Company Act in order to enforce its equi-

\textsuperscript{123} Bromberg, supra note 119, at 468.
\textsuperscript{124} Id. at 480-81.
valent offer policy. There is a demonstrated need for the imposition of the Board's requirement, and sufficient evidence to indicate that it is unlikely to have detrimental effects. Under the Bank Holding Company Act, the Board is required to make an annual report to Congress on the administration of the Act. The Board is also authorized to make "any recommendations as to changes in the law which in the opinion of the Board would be desirable." It is submitted that the Board should propose and Congress should enact an amendment to the Bank Holding Company Act granting the Board authority to deny applications for approval of bank acquisitions by bank holding companies unless substantially equivalent price offers are made to all shareholders.

THOMAS J. FLAHERTY

Truth in Lending—Validity of Four Installment Rule of Federal Reserve Board's Regulation Z—Mourning v. Family Publications Service, Inc.—Petitioner Leila Mourning contracted with Family Publications Service (FPS) for a five-year subscription to four magazines. The petitioner paid $3.95 at the outset and was to make monthly payments of $3.95 for thirty months. Thus, all payments for the sixty-month subscriptions were to have been completed during the first half of the contract term.

The contract contained an acceleration clause whereby on the default of the buyer, the entire balance would become immediately due. Mourning made no further payments after her initial payment, and FPS declared due the balance of $118.50. The contract given Mourning contained no recital of the total purchase price of the subscriptions, the amount due after the initial payment, or the amounts and rates of any service or finance charges. Therefore, alleging that FPS had failed to make the credit disclosures required by the Truth in Lending Act, petitioner brought suit in federal district court for recovery of the statutory penalty for nondisclosure.

The central question in the litigation became the validity of the so-called "four installment" rule of the Federal Reserve Board's Regulation Z, promulgated pursuant to authority granted in section

126 Id.