
Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

Interpretive Letter #891
July 2000
12 USC 214

April 26, 2000

Re: Share Exchanges Pursuant to Model Business Corporation Act ("MBCA")

Dear []:

This is in response to your request for confirmation that a national bank may elect the corporate governance provisions of the MBCA and complete a share exchange in accordance with those provisions. Based on the representations that you have made, we conclude that a bank may effect a share exchange by following the provisions of the MBCA.

Background

The bank would elect the corporate governance provisions of the MBCA through amendment to its articles of association and bylaws, and engage in a share exchange as provided by the MBCA. The bank would form a parent holding company, and the share exchange would ensure that the holding company would own 100 percent of the shares of the bank.

The bank would use several steps to accomplish the share exchange. The bank would form a company to act as the holding company of the Bank.¹ The shareholders of the bank would vote on the plan of share exchange. If the holders of two-thirds of the shares of the bank approve the share exchange, the holding company would then exchange its shares for shares of the bank using the procedures described in the MBCA.² As a result, each shareholder of the bank would own shares of the holding company, and the holding company would own 100 percent of the shares of the bank. Each shareholder of the bank would have the opportunity to own the same

¹ The bank would file an application with the appropriate Federal Reserve Bank to form the holding company.

² See MBCA § 11.02 *et seq.*

number and percentage of shares in the holding company as that shareholder previously held in the bank. In the alternative, shareholders could exercise dissenters' rights and receive cash for their shares.³

Applicable Law

National banks may adopt corporate governance procedures that comply with applicable federal banking law and safe and sound banking practices. An OCC regulation provides that:

To the extent not inconsistent with applicable Federal banking statutes or regulations, or bank safety and soundness, a national bank may elect to follow the corporate governance procedures of the law of the state in which the main office of the bank is located, the law of the state in which the holding company of the bank is incorporated, the Delaware General Corporation Law, Del. Code Ann. Tit. 8 (1991, as amended 1994, and as amended thereafter), or the Model Business Corporation Act (1984, as amended 1994, and as amended thereafter). A national bank shall designate in its bylaws the body of law selected for its corporate governance procedures.⁴

The MBCA expressly permits corporations to conduct share exchanges.⁵ The holders of a majority of each class of shares entitled to vote must approve the plan of share exchange.⁶ The corporation's board of directors also must approve the transaction.⁷ After the shareholders approve the share exchange, the acquiring corporation must deliver articles of share exchange to the secretary of state.⁸

The MBCA requires corporations conducting share exchanges to provide dissenters' rights to shareholders.⁹ Corporations must include notice of dissenters' rights with the notice for the meeting at which the shareholders will vote on the transaction.¹⁰ Any shareholder who wishes to dissent must give notice to the corporation of intent to dissent and may not vote in favor of the transaction at the shareholders' meeting.¹¹ If the shareholders approve the transaction, the corporation must send written notice to all dissenters after the meeting concerning the procedure

³ *See id.* at § 13.01 *et seq.*

⁴ 12 C.F.R. § 7.2000(b)

⁵ MBCA § 11.02(a).

⁶ *Id.* at § 11.03(e).

⁷ *Id.* at § 11.02(a) and 11.03(a)

⁸ *Id.* at § 11.05(a).

⁹ *Id.* at § 13.02(a)(2)

¹⁰ *Id.* at § 13.20(a).

¹¹ *Id.* at § 13.21 (a).

for demanding payment.¹² Dissenting shareholders must then demand payment, and the corporation must make payment to the shareholders.¹³ Any shareholder who is dissatisfied with the payment offered must provide the corporation with an estimate of fair value.¹⁴ The corporation must then either pay the amount requested by the shareholder, or seek an appraisal from the court.¹⁵ In an appraisal proceeding, the corporation is presumed to pay costs, but the court may assess the costs to the shareholders if the court finds that the shareholders' actions were arbitrary, vexatious, or not in good faith.¹⁶

Federal banking law does not expressly address the authority of national banks to engage in share exchanges. There are several mechanisms, however, by which a national bank may form a parent holding company that owns 100 percent of the shares of a bank. For example, a national bank can effect a holding company reorganization by forming a holding company and chartering an interim bank, which is a subsidiary of that company. The existing bank then merges into the interim bank.¹⁷ The National Bank Act provides protection for shareholders in an interim merger by providing dissenters' rights.¹⁸

A national bank may become a holding company subsidiary through other methods, e.g., by forming a holding company which then conducts a tender offer for the shares of the bank. Those methods can be time consuming, relatively expensive, and present a risk that the holding company will acquire less than 100 percent of the bank's shares.

¹² *Id.* at § 13.22.

¹³ *Id.* at §§ 13.23(a) and 13.25(a).

¹⁴ *Id.* at § 13.28(a).

¹⁵ *Id.* at § 13.30(a).

¹⁶ *Id.* at § 13.3 1 (a).

¹⁷ *See* 12 U.S.C. § 215a and 12 C.F.R. § 5.33(e)(4). Some circuit courts have permitted interim mergers. *See, e.g., NoDak Bancorporation v. Clarke*, 998 F.2d 1416 (8th Cir. 1993) (permitting interim merger of national bank that froze out minority shareholders).

¹⁸ *See* 12 U.S.C. § 215a(b)-(d). A dissenting shareholder must either vote against the merger, or give written notice of dissent prior to or at the shareholder meeting at which the shareholders vote on the merger. The value of the dissenting shareholder's shares is determined by an appraisal made by a committee of three persons: one chosen by the dissenting shareholders, one chosen by the directors of the bank (as it exists after the merger), and one chosen by the other two members of the committee. If the committee fails to determine a value of the shares, or a dissenting shareholder is not satisfied with the value determined, the OCC must make an appraisal of the shares. The resulting bank must pay the costs of any appraisal conducted by the OCC.

Discussion

A national bank may adopt MBCA corporate governance procedures and conduct a share exchange, to the extent that those procedures are not inconsistent with applicable federal banking statutes and regulations. OCC regulation expressly permits a national bank to elect the corporate governance procedures of the MBCA.¹⁹

MBCA provisions allowing share exchanges are not inconsistent with applicable federal banking statutes or regulations. MBCA provisions permitting share exchanges are consistent with those provisions in federal banking law that permit national banks to accomplish the same result through different steps where the bank provides adequate dissenters' rights, as described below. To ensure consistency with federal banking law addressing interim mergers,²⁰ national banks that effect a share exchange must provide reasonable appraisal rights to those shareholders who choose not to receive shares by dissenting from the transaction. A national bank conducting a share exchange should provide dissenters' rights that are substantially similar, although not necessarily identical to those in section 215a.²¹

The MBCA provision governing share exchanges provides shareholders with dissenters' rights that are substantially similar to those in section 215a for interim mergers.²² Both the MBCA and section 215a provide shareholders the right to dissent and receive fair value for the shares.²³ In both cases, if the parties are unable to settle on the fair value of the shares, an independent third party (a state court under the MBCA or the Comptroller under the National Bank Act) ultimately determines the fair value of the shares. Under each system of dissenters' rights, a dissatisfied shareholder may dissent from the transaction and receive the fair value of the shares, as determined by the independent third party.

The MBCA in two respects is not consistent with the merger provisions of federal banking law. With regard to dissenters' rights, the MBCA provides that the corporation must pay the cost of any judicial appraisal, unless the court finds that the dissenting shareholders acted arbitrarily, vexatiously, or not in good faith in demanding payment.²⁴ Federal banking law, in contrast, requires the resulting bank to pay for any Comptroller appraisal, without exception.²⁵ Section

¹⁹ 12 C.F.R. § 72000(b).

²⁰ 12 U.S.C. § 215a.

²¹ See Footnote 18, *supra*.

²² MBCA § 13.01 *et seq.*

²³ The scheme of dissenters' rights in the MBCA is also substantially similar to that found in Iowa law. Compare MBCA at § 13.01 *et seq.* with Iowa Code § 490.1301, *et seq.* The OCC has found that the dissenters' rights available under Iowa law afford comparable protections to corresponding provisions in the National Bank Act. See Interpretive Letter No. 786, *reprinted in* [1997 Transfer Binder] Fed. Banking Law Rep. (CCH) ¶ 81-213 (June 9, 1997) and Conditional Approval No. 99-10 (Apr. 1, 1999) at 5.

²⁴ MBCA § 13.31(a).

7.2000(b) limits the ability of national banks to adopt alternative corporate governance to only those statutes that are not inconsistent with federal banking law so that national bank shareholders will not suffer a disadvantage resulting from the bank's selection of that alternative law. To meet that limitation in section 7.2000(b), a national bank proposing to adopt the MBCA and conduct a share exchange must agree to pay the cost of any judicial appraisal that may result. The bank must also agree to pay for arbitration of the matter if the appropriate court refuses jurisdiction of an appraisal action. In addition, any arbitration must be conducted consistent with the rules of the American Arbitration Association or other organization with expertise in alternative dispute resolution.

With regard to the share exchange generally, the MBCA requires approval of the share exchange by a majority of each class of shares entitled to vote.²⁶ Federal banking law, in contrast, requires approval of a merger agreement by the shareholders owning two-thirds of the shares of the bank.²⁷ To ensure that national bank shareholders will not suffer any disadvantage from the difference in approval requirements, a national bank proposing to adopt the MBCA and conduct a share exchange must also agree not to complete the transaction if only shareholders holding less than two-thirds of the shares of the bank approve the transaction.

Conclusion

For the above reasons, and subject to the above conditions, we conclude that the Bank may effect a share exchange pursuant to the MBCA. If you have any questions concerning this letter, please contact Virginia S. Rutledge, Senior Attorney, Securities and Corporate Practices Division, at 202-874-5210.

Sincerely,

-signed-

Julie L. Williams
First Senior Deputy Comptroller and Chief Counsel

²⁵ 12 U.S.C. § 215a(d).

²⁶ MBCA § 11.03(e).

²⁷ See 12 U.S.C. § 215a(a)(2).