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Comptroller of the Currency  
Administrator of National Banks

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Washington, DC 20219

**Conditional Approval #562**  
**January 2003**

December 9, 2002

Craig N. Landrum, Esq.  
Watkins Ludlam Winter & Stennis, P.A.  
6333 North State Street  
Jackson, Mississippi 39202

Re: First American National Bank, Iuka, Mississippi (“Bank”)  
Application Control Number: 2002-SE-12-136

Dear Mr. Landrum:

This responds to the Bank’s application under 12 C.F.R. § 5.46 to elect the corporate governance provisions of Mississippi law and complete a reverse stock split in accordance with those provisions. Based on the representations and commitments made by the Bank, the proposed application is hereby approved, subject to the conditions set forth below.

**A. Background**

**1. Facts**

The Bank is amending its bylaws to elect the corporate governance provisions of Mississippi law to engage in a reverse stock split as permitted by Mississippi law. The Bank proposes the reverse stock split to facilitate an election by the Bank to become a Subchapter S corporation.

The Bank proposes to conduct the reverse stock split through a multi-step process. The Bank will reduce the par value of its shares from the current \$5.00 per share to \$0.40 per share.<sup>1</sup> This will reduce capital stock by \$704,315.20 from \$765,560 to \$61,244.80. The Bank will increase its capital surplus account by the same amount.

The Bank will conduct a reverse stock split at a ratio of 1 to 250 and increase the par value of the shares from \$0.40 to \$100 per share. After the reverse stock split and subsequent increase in par value, 13,830 full shares plus fractional shares totaling 14,813 shares will remain outstanding. In lieu of issuing the fractional shares, the Bank will cash out fractional shares at a price of \$135 per pre-split share, which the board of directors believes is fair. The Bank obtained an

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<sup>1</sup> The Bank currently has 153,112 shares of common stock outstanding at a par value of \$5 per share, which are held by approximately 282 shareholders. After the proposed transaction, the Bank will have approximately 74 shareholders.

independent valuation of its shares from Southard Financial, Memphis, Tennessee. The Bank represents that the valuation will not result in any minority discount on shares.

## 2. Corporate Governance

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.<sup>2</sup>

The OCC has promulgated a regulation, 12 C.F.R. § 7.2023, that codified its decisions permitting reverse stock splits. The OCC confirmed in the regulation the authority of national banks to conduct reverse stock splits where “the transaction serves a legitimate corporate purpose and provides adequate dissenting shareholders’ rights.”<sup>3</sup> The regulation specifically recognizes that reducing the number of shareholders in order to qualify as a Subchapter S corporation is an example of a legitimate corporate purpose supporting a reverse stock split.<sup>4</sup> In the preamble to the rule, the OCC stated its intent was to recognize the flexibility that national banks have to restructure their ownership interests. The OCC also noted the consistency of its regulation with case law recognizing Congressional intent in the National Bank Act to simplify and encourage national bank consolidations.<sup>5</sup>

You have represented that Mississippi law authorizes Mississippi corporations to effect reverse stock splits.<sup>6</sup> Mississippi law expressly requires dissenters’ rights in reverse stock splits.<sup>7</sup> You have represented that the Bank has agreed to provide the dissenters’ rights provided in the Mississippi Business Corporation Act § 79-4-13.01 *et seq.* and to pay the costs of any resulting

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<sup>2</sup> 12 C.F.R. § 7.2000(b).

<sup>3</sup> 12 C.F.R. § 7.2023(a).

<sup>4</sup> 12 C.F.R. § 7.2023(b)(1).

<sup>5</sup> OCC, *Investment Securities; Rules, Policies and Procedures for Corporate Activities; Bank Activities and Operations* (final rule), 64 Fed. Reg. 60092 (Nov. 4, 1999).

<sup>6</sup> Letter from Craig N. Landrum, Esq. to OCC (November 14, 2002).

<sup>7</sup> See Miss. Code Ann. § 79-4-13.02(4).

appraisal. You have also represented that the Bank will provide for binding arbitration if a court declines to accept jurisdiction in any action seeking appraisal.

The Bank will give prior notice of dissenters' rights to shareholders before the shareholder meeting acting on the proposal, pay the cost of any appraisal in a court proceeding, and provide for binding arbitration if a court declines to accept jurisdiction in any action seeking appraisal.

## **B. Discussion**

The Bank may adopt Mississippi corporate governance procedures to the extent that those procedures are not inconsistent with applicable Federal banking statutes or regulations. OCC regulations expressly permit a national bank to elect the corporate governance procedures of the law of the state in which the main office of the bank is located.<sup>8</sup> The Bank may elect Mississippi corporate governance procedures because the main office of the Bank is located in Mississippi.

The Bank represents that reverse stock split transactions are permitted under Mississippi law, and are consistent with applicable Federal banking statutes or regulations. No provision of Federal law expressly prohibits reverse stock splits. Several provisions of the National Bank Act authorize the elements of a reverse stock split and, when read together, allow a national bank to engage in a reverse stock split for a legitimate corporate purpose if the bank provides adequate dissenting shareholder rights.<sup>9</sup> Based on these authorities, the OCC has promulgated a regulation expressly permitting reverse stock splits if the transaction serves a legitimate corporate purpose and provides adequate dissenting shareholders' rights.<sup>10</sup>

After reducing the par value of the Bank's shares to comply with 12 U.S.C. § 52, the Bank proposes to amend its articles of association to decrease the number of authorized shares of common stock and to increase the par value of each resulting share. Banks may amend their articles of association by the vote of the holders of a majority of the voting shares of stock to determine the number and par value of bank shares.<sup>11</sup> The National Bank Act permits a national bank to reduce its capital upon the vote of shareholders holding two-thirds of its capital stock and OCC approval.<sup>12</sup>

The Bank next proposes to replace each of the outstanding shares of common stock with new common stock at the rate of one share of new common stock for each 250 shares of outstanding

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<sup>8</sup> See 12 C.F.R. § 7.2000(b).

<sup>9</sup> See OCC Advisory Letter No. 2002-6 (July 17, 2002)(Reverse Stock Split Procedures); Conditional Approval 434 (Dec. 15, 2000); Interpretive Letter No. 786 (June 9, 1997), *reprinted in* [1997 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-213; and Interpretive Letter No. 275 (Oct. 21, 1983), *reprinted in* [1983-84 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,439.

<sup>10</sup> See 12 C.F.R. § 7.2023.

<sup>11</sup> See 12 U.S.C. § 21a; *see also* 12 U.S.C. § 52 (par value may not exceed \$100 per share).

<sup>12</sup> See 12 U.S.C. § 59.

common stock. The Bank will pay cash for any fractional shares outstanding. National banks have express authority to pay the cash equivalent of fractional shares of stock.<sup>13</sup> The cash equivalent must be based on the market value of the stock or, if no market exists, a reliable and disinterested determination as to the fair market value of the stock.<sup>14</sup>

Judicial authority provides support for concluding that reverse stock splits for legitimate corporate purposes are consistent with the National Bank Act, where banks provide appropriate dissenters' rights. While the only Federal Court of Appeals case to address reverse stock splits directly, *Bloomington Nat'l Bank v. Telfer*, decided on the facts that the transaction before it violated the National Bank Act, the court declined to determine if reverse stock splits would be permissible for valid business purposes if dissenting shareholders' rights were provided.<sup>15</sup> The court also noted that the decision was limited to the facts of the case.<sup>16</sup>

In *NoDak Bancorporation v. Clarke*, the Eighth Circuit held that national banks could effect freeze-out mergers to allow a holding company to obtain 100 percent ownership so long as the national bank has a valid corporate purpose and observes dissenters' rights.<sup>17</sup> The NoDak court found that a national bank may engage in any merger not inconsistent with 12 U.S.C. 214a and 215-215a, and that freeze-out mergers are consistent with those sections.<sup>18</sup> More recently, a district court in the Tenth Circuit relied on *NoDak* to hold that a bank may effect a freeze-out merger to consolidate with another bank and become a wholly-owned subsidiary of an existing bank holding company.<sup>19</sup>

In *Lewis v. Clark[e]* the Eleventh Circuit determined that a national bank may not offer different consideration to shareholders when the bank effects a freeze-out merger under 12 U.S.C. § 215a.<sup>20</sup> The court held that the OCC lacked authority to approve mergers where minority shareholders receive cash for their shares and majority shareholders receive stock in the resulting bank, even in cases where the minority shareholders have appraisal rights. That case did not involve a decision, like the present case, where a regulation expressly permits reverse stock splits. Since the OCC has adopted section 7.2023 following a notice and comment

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<sup>13</sup> See 12 C.F.R. § 5.67(c).

<sup>14</sup> "The cash equivalent is based on the market value of the stock, if there is an established and active market in the national bank's stock." See *id.* In the absence of an established and active market in the Bank's stock, the Bank obtained an independent valuation as to the fair market value of its shares.

<sup>15</sup> *Bloomington Nat'l Bank v. Telfer*, 916 F.2d 1305 (7th Cir. 1990) ("*Bloomington*").

<sup>16</sup> See *id.*, 916 F.2d at 1308 n.4, 1309.

<sup>17</sup> *NoDak Bancorporation v. Clarke*, 998 F.2d 1416 (8th Cir. 1993) ("*NoDak*").

<sup>18</sup> See *id.*, 998 F.2d at 1419-20 and 1425.

<sup>19</sup> See *Moody v. First National Bank, Sallisaw*, CV-00-306-5 (E.D.Ok. July 5, 2001).

<sup>20</sup> *Lewis v. Clark[e]*, 911 F.2d 1558 (11th Cir. 1990), *reh'g denied*, 972 F.2d 1351 (1991) ("*Lewis*").

procedure, courts reviewing an OCC decision approving a reverse stock split should give deference to the OCC's reasonable interpretation of a statute that it administers.<sup>21</sup> Moreover, the OCC has permitted national banks to conduct reverse stock splits in numerous situations since *Lewis* and *Bloomington* were decided. In the period since *Lewis* and *Bloomington*, the OCC has approved reverse stock splits for banks located in fourteen states in cases where the banks had legitimate corporate purposes in conducting the transactions.<sup>22</sup> Thus, applicable statutory and regulatory provisions and the majority of judicial precedent would permit reverse stock splits for legitimate business purposes, provided dissenters' rights are available.

The Bank has articulated legitimate business purposes in effecting a reverse stock split. The Bank intends to become a Subchapter S corporation. Qualification for Subchapter S status requires achieving the required maximum number of shareholders.<sup>23</sup> Accordingly, the Bank can pursue the reverse stock split to qualify as a Subchapter S corporation. Eliminating burdens associated with a shareholder constituency is a proper business purpose.<sup>24</sup> It also is a valid business purpose to effect a merger in order to reduce corporate expenses associated with shareholder communications and meetings.<sup>25</sup> The OCC expressly recognizes these corporate purposes in its regulation permitting national banks to conduct reverse stock splits.<sup>26</sup>

To avoid undermining the purposes of 12 U.S.C. §§ 214a and 215-215a, however, a reverse stock split must provide shareholders reasonable dissenters' rights to ensure that they receive a fair price for their shares. Those dissenters' rights need not be identical to those located in sections 214a, 215, and 215a. Accordingly, the Bank may effect a reverse stock split as long as it has a valid corporate purpose for the transaction and observes appropriate dissenters' rights.

Minority shareholders in the reverse stock split will receive dissenters' rights comparable to those under the National Bank Act in mergers and consolidations.<sup>27</sup> Specifically, the Bank has

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<sup>21</sup> *United States v. Mead Corp.*, 533 U.S. 218 (2001); *Christensen v. Harris County*, 529 U.S. 576 (2000).

<sup>22</sup> See Advisory Letter 2002-6, *supra*; Conditional Approval 541 (July 30 2002).

<sup>23</sup> See 26 U.S.C. §§1361(b)(1)(A) and 1362(a)(2).

<sup>24</sup> See *Leader v. Hycor, Inc.*, 479 N.E.2d 173, 178 (Mass. 1985); see also *Nash v. Farmers New World Life*, 1976 U.S. Dist. 15,846, \*48 (S.D. Ohio, 1976).

<sup>25</sup> See *Teschner v. Chicago Title & Trust Co.*, 322 N.E.2d 54,58 (Ill. 1974).

<sup>26</sup> 12 C.F.R. § 7.2023(b).

<sup>27</sup> Under the National Bank Act, 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 shareholders' 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. See 12 U.S.C. §§ 214a(b), 215(b)-(d), and 215a(b)-(d).

represented that it will provide notice of dissenters' rights to the minority interest holders before the shareholder meeting acting on the reverse stock split proposal; pay the cost of an independent third party appraisal of the shares if the Bank and any dissenting shareholders are unable to agree on the value of the dissenting shares; and pay the cost of a binding arbitration by an independent third party, if the court that would ordinarily hear an appraisal action under the corporate governance procedures refuses jurisdiction to appraise the shares of a national bank.

Mississippi law in one respect is not consistent with the dissenters' rights available in federal banking law. Mississippi law 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.<sup>28</sup> Federal banking law, in contrast, requires the resulting bank to pay for any Comptroller appraisal, without exception.<sup>29</sup> Section 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 Mississippi law and conduct a share exchange must agree to pay the cost of any judicial appraisal that may result. The Bank has agreed to do so, and to pay for arbitration of the matter if the appropriate court refuses jurisdiction of an appraisal action.

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Mississippi law effectively provides for dissenters' rights in connection with reverse stock splits because it provides for dissenters' rights when there is an amendment to the articles of incorporation that reduces the number of shares held by a shareholder to a fraction of a share if the corporation will then acquire that fractional share. Miss. Code Ann. § 79-4-13.02(4)(v). Corporations must include notice of dissenters' rights with the notice for the meeting at which the shareholders will vote on the transaction. *Id.* at § 79-4-13.20(a). 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. *Id.* at § 79-4-13.21(a). If the shareholders approve the transaction, the corporation must send written notice to all dissenters after the meeting concerning the procedure for demanding payment. *Id.* at § 79-4-13.22(a). Dissenting shareholders must then demand payment, and the corporation must make payment to the shareholders. *Id.* at §§ 79-4-13.23(a) and 79-4-13.24(a). Any shareholder who is dissatisfied with the payment offered must provide the corporation with an estimate of fair value. *Id.* at § 79-4-13.28(a). The corporation must then either pay the amount requested by the shareholder, or seek an appraisal from the court. *Id.* at § 79-4-13.30(a).

The dissenters' rights for Bank shareholders will afford protections comparable to the dissenters' rights provisions in the National Bank Act. Under both provisions, a minority shareholder in a reverse stock split has the right to dissent and receive fair value for the shares. If the parties are unable to settle on the fair value of the shares, a state court (under Mississippi law) or the Comptroller (under the National Bank Act) ultimately determines the fair value of the shares. The Bank has agreed to pay the appraisal costs in a court action. If the state court that would ordinarily hear the appraisal action refuses jurisdiction in the matter, the Bank will pay the costs of a binding arbitration by an independent third party.

<sup>28</sup> Miss. Code Ann. § 79-4-13.31.

<sup>29</sup> 12 U.S.C. § 215a(d).

### **C. Conclusion**

For the above reasons, including the representations and commitments made by the Bank, we find that the reverse stock split application is legally authorized and meets the other statutory criteria for approval. Accordingly, this application is hereby approved, subject to the following conditions:

1. The Bank will elect the corporate governance provisions of Mississippi law.
2. The Bank will provide for dissenters' rights comparable to those found in 12 U.S.C. §§ 214a, 215, and 215a.
3. If any shareholders dissent from the reverse stock split, the Bank will pay the cost of any appraisal that may occur.
4. If the appropriate court(s) decline to accept jurisdiction of an appraisal action, the Bank will provide for binding arbitration to conduct an appraisal by an independent third party.

Please be advised that the above conditions of this approval shall be deemed to be conditions "imposed in writing by the agency in connection with the granting of any application or other request" within the meaning of 12 U.S.C. § 1818(b)(1).

Please notify the OCC when the change in capital has been completed in accordance with this approval. The notification should state the date of the change, and the dollar amount of the reduction in the common stock and surplus account associated with the payment for fractional shares. The notification should include a certification that shareholders approved the change in capital structure according to law, regulations, and the Bank's Articles of Association. A secretary's certificate of shareholder approval and a certified copy of the amendment to the Articles of Association should be included. The notification also should include a statement that the change in the capital structure complies with all applicable laws and regulations. Upon receipt of the notification, the OCC will review the reduction in capital attributable to the payment for fractional shares.

If the reverse stock split is not consummated within one year from the approval date, the approval shall automatically terminate unless the OCC grants an extension of the time period. Please advise Louis Gittleman, Senior Licensing Analyst, within 10 days of the effective date of the reverse stock split.

Please include the CAIS control number on all correspondence related to this application.

This approval, and the activities and communications by OCC employees in connection with the filing, do not constitute a contract, express or implied, or any other obligation binding upon the OCC, United States, any agency or entity of the United States, or any officer or employee of the United States, and do not affect the ability of the OCC to exercise its supervisory, regulatory and

examination authorities under applicable laws and regulations. The foregoing may not be waived or modified by any employee or agent of the OCC or the United States.

If you have any questions, please contact Louis Gittleman, Senior Licensing Analyst, at 404-588-4525.

Sincerely,

**-signed-**

Steven J. Weiss  
Deputy Comptroller for Licensing