

IN THE UNITED STATES DISTRICT COURT  
FOR THE WESTERN DISTRICT OF MISSOURI  
WESTERN DIVISION

STEVEN CHASE, and )  
SHAWN PENNER, )  
 )  
Plaintiffs, )  
 )  
v. )  
 )  
FIRST FEDERAL BANK OF )  
KANSAS CITY, et al., )  
 )  
Defendants. )

No.: 4:17-cv-00094-DGK

**MOTION OF AMERICAN BANKERS ASSOCIATION AND MISSOURI BANKERS ASSOCIATION TO FILE BRIEF *AMICI CURIAE* IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS THE FIRST AMENDED CLASS ACTION COMPLAINT**

The American Bankers Association ("ABA") and the Missouri Bankers Association ("MBA", and collectively, the "Movants") respectfully request leave to file a brief *amicus curiae* in the above-captioned matter.

The Movants sought consent from the parties for filing their *amicus curiae* brief. Counsel for Defendants gave consent, but counsel for Plaintiffs took no position on this motion to file a brief *amicus curiae* and reserved all of their rights, including the right to oppose this motion.

**I. INTRODUCTION**

With the vast majority of the nation's 520 mutual banks among its members, the ABA is the preeminent national organization for mutual institutions. In fact, 8.8% of all U.S. banks are mutual, and 12.1% of ABA's membership is made up of mutuals. Mutual community bankers play a leading role in ABA's leadership: Three members of the ABA Board of Directors, including the 2016-2017 ABA Chairman and ABA Treasurer, lead mutually chartered banks or

holding companies. In addition, a 15-member Mutual Institutions Executive Committee leads the 141 ABA Member Mutual Institutions Council. ABA's annual Mutual Community Bank Forum is the only national meeting dedicated solely to mutual institutions. ABA is proud to represent and support its mutually chartered institutions.

The MBA is a Missouri non-profit corporation that was established as a trade association to promote the interests of the banking industry and the general welfare and usefulness of banks and banking institutions. Founded in 1891, MBA represents more than 275 member banks and savings banks located in Missouri with more than 2,000 locations in Missouri and employing over 30,000 Missouri residents. There are nine mutual savings banks in Missouri, and seven of these mutual institutions are MBA members. MBA is the principal advocate for the banking industry in Missouri and dedicates its efforts to protecting the interests of its members and promoting a fair and competitive banking environment.

Neither the ABA nor the MBA have any parent companies, subsidiaries, or affiliates that have issued shares to the public.

## **II. ARGUMENT**

"A district court has broad inherent authority to permit or deny an appearance as *amicus curiae*." *United Fire & Casualty Co. v. Titan Contractors Services, Inc.*, No. 4:10-cv-2076-CAS, 2012 WL 3065517, \*6 (E.D. Mo. July 27, 2012). "The function of an *amicus curiae* is to call the court's attention to law, facts, or circumstances in a matter then before it that may otherwise escape its consideration." *Pettet v. May*, No. 2:11-cv-04049-NKL, 2011 WL 3354089, \*4 (W.D. Mo. Aug. 3, 2011).

The Court would benefit from the viewpoint and argument of ABA and MBA because the issues raised in this lawsuit are paramount to the operations of mutual banks. Because a

mutual banking institution does not have access to investor capital, the mutual banks' retained earnings provide the primary means to grow and thrive and to survive economic hard times. Capital is critical to a banking institution's safety and soundness and is the first measure of soundness that state and federal bank examiners evaluate in their regular examinations. The plaintiffs in this case present a grave threat to mutual banks and to the communities that depend on these institutions.

Permitting the ABA and MBA to participate in this case is appropriate because the interests of non-party mutuals, as well as the communities they serve, would otherwise not be represented, and the interests of said financial institutions and communities will be negatively impacted if Plaintiffs succeed on their claims.

The ABA and MBA seek to file this brief in support of Defendants' Motion to Dismiss. By an order dated March 3, 2017, Defendants' responsive pleading deadline is May 1, 2017. The ABA and MBA are submitting this Motion, with the attached brief *amicus curiae*, on the date of Defendants' filing of their Motion to Dismiss, allowing Plaintiffs adequate time to respond.

For the foregoing reasons, the ABA and MBA respectfully request that this Court grant it leave to file the attached brief *amicus curiae* in support of Defendants' Motion to Dismiss.

Respectfully submitted,

/s/ George F. Verschelden  
George F. Verschelden MO Bar # 55128  
STINSON LEONARD STREET LLP  
1201 Walnut St., Suite 2900  
Kansas City, Missouri 64106  
Tel: (816) 842-8600  
Fax: (816) 691-3495  
george.verschelden@stinson.com

ATTORNEY FOR THE AMERICAN BANKERS  
ASSOCIATION AND THE MISSOURI BANKERS  
ASSOCIATION

**CERTIFICATE OF SERVICE**

The undersigned attorney hereby certifies that on this 1<sup>ST</sup> day of May, 2017, the foregoing document was filed with the Clerk of the Court by using the CM/ECF system, which sent notification of such filing to all counsel of record.

/s/ George F. Verschelden  
Attorney for the American Bankers Association and  
the Missouri Bankers Association

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ASSOCIATION AS *AMICI CURIAE* IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS  
THE FIRST AMENDED CLASS ACTION COMPLAINT**

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## **INTRODUCTION**

A mutual bank's retained capital is the equivalent of a farmer's seed corn. It provides for future growth and is the store that carries the bank through lean years. Capital is critical to a banking institution's safety and soundness and is the first measure of soundness that state and federal bank examiners evaluate in their regular examinations. Because a mutual banking institution does not have access to investor capital, a mutual bank's retained earnings provide the primary means to grow and thrive and to survive economic hard times. The plaintiffs in this case seek a windfall payout of the surplus of Inter-State Federal Savings & Loan Association of Kansas City ("Inter-State") that has been accumulated in the bank and invested in the community since 1889. Accepting plaintiffs' position would present grave consequences to mutual banks and to the communities that depend on these institutions.

Because the putative class has no enforceable "ownership" interest in Inter-State or call on capital, holding only a liquidation interest, *Amici* seeks to provide this court with information concerning the history and benefits of the community based mutual charter, the benefits and safety provided by capital, and the detrimental impact that plaintiffs' position would have on mutual institutions, including *Amici's* members.

### **I. BACKGROUND**

#### **A. AMERICAN BANKERS ASSOCIATION**

With the vast majority of the nation's 520 mutual banks among its members, the American Bankers Association ("ABA") is the preeminent national organization for mutual institutions. In fact, 8.8% of all U.S. banks are mutual, and 12.1% of ABA's membership is made up of mutuals. Mutual community bankers play a leading role in ABA's leadership: Three members of the ABA Board of Directors, including the 2016-2017 ABA Chairman and ABA Treasurer, lead mutually chartered banks or holding companies. In addition, a 15-member Mutual Institutions Executive

Committee leads the 141 ABA Member Mutual Institutions Council. ABA’s annual Mutual Community Bank Forum is the only national meeting dedicated solely to mutual institutions. ABA is proud to represent and support its mutually chartered institutions.

## **B. MISSOURI BANKERS ASSOCIATION**

The Missouri Bankers Association (“MBA”), founded in 1891, is a statewide association that advocates for and represents 275 member banks and savings banks located in Missouri. MBA banks employ more than 30,000 people. Seven of the nine mutual savings banks in Missouri are MBA members. The MBA promotes member banks’ interests. Community banks are vital to the state’s economy and to the communities these banks serve. Mutual savings banks are not just community based but are effectively community owned.

## **C. HISTORY OF MUTUAL BANKS**

The mutual form of ownership is almost as old as the nation itself. The first two, Philadelphia Savings Fund Society and the Provident Institution for Savings, date their creation to 1816 with doors open and accepting deposits in 1817.<sup>1</sup> A savings bank wave swept through cities and towns of the east—savings banks were established in Baltimore, Maryland and Salem, Massachusetts, in 1818; in Hartford, Connecticut, and Providence and Newport, Rhode Island, in 1819; and Albany, New York, in 1820.

During this time, mutual savings associations were organized to assist the working and lower classes by providing a safe place to deposit money and earn interest.<sup>2</sup> Workers could deposit as little as five cents and could withdraw the monies as needed. Importantly, the collective pooling of these modest resources allowed these workers to borrow money, improve their lives, and help their communities grow. As Thomas Eddy put it, savings banks “are certainly most

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<sup>1</sup> Weldon Welpling, *Mutual Savings Banks* 8, 10 (1968).

<sup>2</sup> Fed. Deposit Ins. Corp., *An Examination of the Banking Crises of the 1980s and Early 1990s*, at 211 (1997), available at [https://www.fdic.gov/bank/historical/history/211\\_234.pdf](https://www.fdic.gov/bank/historical/history/211_234.pdf).

admirably calculated to be beneficial to the poor, by promoting among them a spirit of independence, economy, and industry.”<sup>3</sup> These first mutual savings associations, started as philanthropies, were mutually owned—the trustees held no ownership and took no dividend. “The greatest good,” wrote the Secretary of Boston’s Provident Institution for Savings, “is in affording the humble journeymen, coachmen, chamber-maids, and all kinds of domestic servants, and inferior artisans, who constitute two-thirds of our population, a secure disposal of their little earnings, which would otherwise be squandered.”<sup>4</sup>

The granting of the original mutual charters required an act of the state legislature. Likewise, amendments to charters required state acts. Some charters mandated the amount of interest to be paid to depositors and the amount that depositors could place with the savings banks. For instance, the Philadelphia Savings Fund Society’s initial charter limited the amount of deposit to \$500 per year and included an overall limitation on the dollar amount of deposits that could be accepted to \$300,000.<sup>5</sup> Changes required legislative action, a cumbersome process. Even the ability to offer mortgages required a charter amendment and legislative action for the early mutual savings banks.<sup>6</sup>

But the savings banks grew fast. By 1860, deposits in savings banks reached about \$150 million and were held by approximately 700,000 depositors.<sup>7</sup> Indeed, this growth, and financial panics in 1837 and 1857, moved the chartering of savings banks by legislation to the enactment of general laws to apply uniform powers and authorities to savings banks in a given state. As Welfling explains, “by the end of the Civil War period, however, general laws typically

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<sup>3</sup> James Hilton Manning, *Century of American Savings Banks* 114 (1917).

<sup>4</sup> Weldon Welfling, *Money and Banking: A First Course* 285 (1947).

<sup>5</sup> *Id.* at 9.

<sup>6</sup> See Emerson W. Keyes, *A History of Savings Banks in the United States* 341-347 (N.Y. Bradford Rhodes, 1876).

<sup>7</sup> Welfling, *supra* note 1, at 27.

superseded charters as sources of bank powers and regulation.”<sup>8</sup> Legislation had simply become too cumbersome a process for bank regulation.

The evolving history of the mutual charter illustrates why and how the elegant and archaic language of Inter-State’s charter came to be in 1889. Early charters were replete with references to benefits for savers of small means. With the adoption of a general law, charter language became less poetical and inspirational. General laws also moved the supervision of banking from a legislative function to an executive function that was better able to adjust to the needs of customers, communities, and the institutions themselves as economic conditions warranted.

## **II. ARGUMENT**

### **A. THERE ARE IMPORTANT DIFFERENCES BETWEEN MUTUAL AND STOCK INSTITUTIONS THAT IMPACT GOVERNANCE**

Mutual savings banks are community focused institutions just like stock community banks. What makes mutuals different, however, is their unique attachment, as a non-stock institution, to the communities they serve and their longevity.<sup>9</sup> It is paramount for a mutual institution to focus on the needs of a local township or city—as the short term quarterly return is not a driving force for a non-stock institution. A mutual bank can assess the needs of the local community and participate in it over a longer time horizon without criticism or market pressures. It can invest in new products and services and thereby benefit its depositor and borrower base.

As communities grow, mutual banks also grow. Often, the mutual institution is one of, if not the only, hometown bank in the community. And not only do mutual institutions help businesses capitalize, but they serve as a catalyst for transformation. This philosophy has yielded

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<sup>8</sup> *Id.* at 29.

<sup>9</sup> See OCC Bulletin 2014-35 (July 22, 2014). “Free from stockholder calls for larger returns, mutual institutions still tend to be small, locally focused institutions that are woven into the fabric of the communities they serve. The OCC tailors its examination procedures and off-site monitoring systems to the unique characteristics and operations of these institutions. Mutuals continue to play an important role in providing financial services to communities across America.” *Id.*

countless success stories, from a local dry cleaner who has added innovative new business offerings, to a family-owned farm now functioning as a new event space and agri-tourism destination.<sup>10</sup> Aside from the need to be competitive and profitable, mutual institutions demonstrate a responsiveness to community that goes well beyond profits and strives to improve the quality of life. In essence, the heart of a mutual institution is its community factor.

First Federal Bank of Kansas City (“First Federal”)—the bank Inter-State merged with—is a prime example, having survived wars, depression, and major crises by having more than sufficient capital. The bank’s core belief is giving back to non-profit organizations and educational institutions that strengthen vital community needs, such as economic development, education and youth activities, arts and culture, and health and human services.<sup>11</sup> In fact, the bank donates 5.5% of the bank’s pre-tax profit to charitable causes, which amounted to \$180,000 this past fiscal year.

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<sup>10</sup> *Here are Some of the 10,000 Business Banking Stories We Help to Tell*, Union Sav. Bank, <https://www.unionsavings.com/business/customer-stories> (last visited May 1, 2017).

<sup>11</sup> First Federal’s community outreach on economic development includes supporting, amongst many others, the Hillcrest Transitional Housing and Bright Futures Fund, which address the financial, housing, and education needs of minority and low and moderate income individuals and families. Second, the bank invests in the education of youth by providing scholarships to graduating high school seniors within the bank’s market area. Third, the bank supports arts organizations and cultural institutions, such as Arts KC and the Children’s Center for the Visually Impaired, that provide cultural opportunities to underserved populations through theatre, music, and visual arts. Finally, the bank supports programs that address hunger, homelessness, and emergency services, such as Habitat for Humanity, Harvesters Community Food Network, and the Healing House. On top of all this, last year the bank’s employees volunteered hundreds of hours to charities and community organizations, from landscaping at area cemeteries in preparation for Memorial Day, making care packages for participants in local charity races, and visiting seniors in hospice care. *See Charitable Giving*, First Fed. Bank of Kansas City, [http://www.ffbk.com/about\\_us/charitable\\_giving.aspx](http://www.ffbk.com/about_us/charitable_giving.aspx) (last visited May 1, 2017); *see also* Newsletter, First Fed. Bank of Kansas City (Winter 2017), <http://www.ffbk.com/sites/www/Uploads/Files/About%20Us/Newsletter.pdf>.

## **B. ADEQUATE CAPITAL IS FUNDAMENTAL TO SAFE AND SOUND BANKING**

Mutual institutions are governed by boards of directors that set policies and oversee management's operation of the savings bank. The board of directors, along with management, is charged with managing and overseeing the mission of a mutual institution. This includes determining appropriate capital levels and activities within supervisory restraints. Also within their purview are decisions about corporate organization and the best means to serve the interest of their communities. The members of the board of directors are not subject to the pressures of stockholders who are interested in maximizing shareholder value, but instead maintain their focus on preserving a robust mutual community bank that serves the community.

In the area of capital, the federal requirements are extensive<sup>12</sup> and are considered “an essential component in determining the safety and soundness” of mutual institutions the FDIC insures and supervises.<sup>13</sup> That a banking institution be well capitalized is fundamental to safe and sound banking. Minimum regulatory capital levels are thresholds. In particular, the FDIC encourages “banks to maintain capital well above the minimums.”<sup>14</sup> Failure to maintain requisite capital levels subjects an institution to a host of adverse actions, including capital restoration plans, capital directives, cease and desist orders, civil money penalties, individual minimum capital requirements, restrictions on the payment of capital distributions and management fees, growth

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<sup>12</sup> *E.g.*, 12 C.F.R. pt. 325.

<sup>13</sup> 12 C.F.R. § 325.1. And for federally chartered mutual savings banks the OCC recognizes only the “liquidation” interest that depositors have in the capital of the mutual at 12 C.F.R. § 5.21(e) “section 8” of the charter form. Even if a mutual converts to a stock form or merges into a stock bank, depositors do not have a call on capital. In this instance the institution must establish a “liquidation account” for each existing depositor for so long as that deposit continues for contingent distribution in a liquidation. *See* 12 C.F.R. §§ 192.450, *et seq.*

<sup>14</sup> 12 C.F.R. pt. 325, App. B - Statement of Policy on Capital Adequacy.

restrictions, transaction prior approvals, additional borrower restrictions, and a host of restrictions and limitations on the operations of the bank.<sup>15</sup>

The demands of plaintiffs would put directors of mutual institutions in an untenable position. On one hand, the directors could reject the depositors' demand to the distribution of accumulated surplus, thereby exposing themselves to liability. On the other hand, the directors could acquiesce to the depositors' demand, thereby making the institution vulnerable to unforeseen economic downturns. This situation would have a discouraging effect of deterring qualified director candidates from serving. As the FDIC has acknowledged, banks must "be able to attract and to retain experienced and conscientious directors and officers" to steer their institutions on a "sound and prudent" path. FDIC, *Statement Concerning the Responsibilities of Bank Directors and Officers* (1992).<sup>16</sup> In other words, asking directors to distribute accumulated surplus built over generations at the whim of activist depositors puts directors to a Hobson's choice and potentially threatens the survivability of mutual institutions.<sup>17</sup> As stewards of a community resource, directors could not effectively steer their bank on a "sound and prudent" path if capital harvesters raid the bank's capital and thereby undermine the bank's continued viability to serve its community.

In this case, the attempt to appropriate a portion of Inter-State's capital fails to recognize the greater national concerns of the Federal Deposit Insurance Fund and the regulatory requirements of both the FDIC and the OCC for the safe and sound operation of the institution. Rather, it is an attempt by a self-interested group to benefit only itself. It should be rejected.

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<sup>15</sup> 12 C.F.R. § 325.105.

<sup>16</sup> Available at <https://www.fdic.gov/regulations/laws/rules/5000-3300.html>.

<sup>17</sup> In any event, the Director Defendants are powerless on their own to make a capital distribution of the magnitude sought by Plaintiffs. Federal law requires OCC approval as a condition precedent to such a distribution. 12 C.F.R. § 5.55.

### **C. MUTUAL BANKS TEND TO HAVE HIGHER CAPITAL LEVELS BECAUSE OF THEIR RELIANCE ON RETAINED EARNINGS**

Unlike commercial institutions that can raise capital via a stock issue, mutual institutions support their growth almost exclusively by retained earnings. Commercial banks with access to national markets can issue new capital instruments to meet regulatory demands or to meet capital needs in times of stress. However, mutual institutions are dependent on retained earnings because they lack access to equity and credit markets and thus are often unable to raise new capital.<sup>18</sup>

Mutual institutions are highly sensitive to the risk of being labeled undercapitalized by their regulators due to the limited or cumbersome options to increase capital other than by retained earnings. Given the supervisory consequences of holding too little capital, the rational response for mutual institutions is to hold more capital than might ultimately be required even beyond a “well capitalized” status. This is an approach that has been supported by the bank regulators as part of the CAMELS supervisory rating each institution receives after its safety and soundness examination. The first ratings element, “C” in CAMELS, specifically assigns a rating the capital position of the institution.<sup>19</sup>

Plaintiffs assert that the minimum 8 percent capital-to-asset ratio is sufficient. Am. Compl. ¶ 22. Plaintiffs are wrong. The minimum capital requirement is a floor and much higher capital

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<sup>18</sup> Pledged deposits are cumbersome and rarely, if ever used. Mutual capital certificates are also a rare and remote possibility, but no institution has successfully used the technique since the 1970s. OCC Bulletin 2014-35 (July 22, 2014), *available at* <https://www.occ.treas.gov/news-issuances/bulletins/2014/bulletin-2014-35.html>. Hence the need for new legislative authority from Congress.

<sup>19</sup> The Uniform Financial Institutions Rating System (UFIRS) was adopted by the Federal Financial Institutions Examination Council (FFIEC) on November 13, 1979. Over the years, the UFIRS has proven to be an effective internal supervisory tool for evaluating the soundness of financial institutions on a uniform basis and for identifying those institutions requiring special attention or concern. The six key components used to assess an institution's financial condition and operations are: capital adequacy, asset quality, management capability, earnings quantity and quality, the adequacy of liquidity, and sensitivity to market risk. Uniform Financial Institutions Rating System, 62 Fed. Reg. 752 (Jan. 1, 1997). All federal banking regulatory agencies and most state bank regulatory agencies utilize this rating system.

ratios are preferred, particularly for mutual institutions. Following the merger, First Federal’s capital ratios were well within the range of capital ratios seen at other mutual institutions. For example, after the fourth quarter of 2016, First Federal’s Tier 1 Capital Ratio stood at 35.39%. The average for mutuals was 29.35%, many multiples above the 8% minimum standard to be considered “well capitalized.”<sup>20</sup>

<b>Ratio</b>	<b>Well-Capitalized Standard</b>	<b>First Federal</b>	<b>Average</b>
Tier 1 Capital	8%	35.39%	29.35%
Leverage	4%	17.21%	14.83%
Total Capital	10%	35.89%	30.37%

In comparison to First Federal, 92 mutual savings banks held a higher Tier 1 Capital Ratio, 98 mutual savings banks held a higher Leverage Ratio, and 97 mutual savings banks held a higher Total Capital Ratio.<sup>21</sup> First Federal is not an outlier for holding accumulated capital well above the existing capital standards. Mutual savings banks recognize the difficulty and long term focus required to raise capital through retained earnings.

The need for capital is well documented through the “Great Recession” of 2008 and the financial crises associated with this event. While that crisis gave rise to the Dodd-Frank Act (2010), it was presaged by the savings and loan crisis in the 1980s which prompted the enactment of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA). Under FIRREA, the federal deposit insurance program for thrifts and savings banks (Federal Savings and Loan Insurance Fund – FSLIC) was reformed and designated the Savings Association Insurance Fund (SAIF). Ultimately, to strengthen the savings bank insurance program, the fund was consolidated and merged with the bank deposit insurance fund under the control of the FDIC and

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<sup>20</sup> Calculated by S&P Global Market Intelligence; SNL Financial Data.

<sup>21</sup> *Id.*

the need for stronger bank capital standards was reinforced.<sup>22</sup> The federal banking agencies, including the FDIC, were given great authority to set capital standards both generally and more specifically through the imposition of Individual Minimum Capital Requirements.<sup>23</sup> As noted in the conference report accompanying FIRREA:

Capital also protects the deposit insurance fund by providing a cushion against losses if the institution's condition deteriorates. Even the most prudently managed savings association may experience losses, such as through changes in interest rates, a downturn in the local economy, or unfortunate investment decisions. An institution with adequate capital should be able to absorb such losses.<sup>24</sup>

If plaintiffs are allowed to raid the bank's capital, then the bank will be placed in an untenable position between Scylla and Charybdis—the financial regulators who determine whether the bank is safe and sound and the bank depositors sweeping capital out of the bank. This threatens the economic viability of the bank and its long term existence and starves it of the financial capital needed to serve its community and the customers who depend on its financial well-being. The Court should reject plaintiffs' opportunistic position and follow the legal and regulatory framework that has developed over more than a century to assure safe and sound mutual institutions that serve our community today and will continue to do so in the future.

### **CONCLUSION**

For the foregoing reasons, *Amici* request that the Court grant Defendants' motion to dismiss Plaintiff's First Amended Class Action Complaint.

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<sup>22</sup> FDIC, Financial Institution Letter on Merger of Bank Insurance Fund and Savings Association Insurance Fund (Apr. 27, 2006), available at <https://www.fdic.gov/news/news/financial/2006/fil06036.html>.

<sup>23</sup> FDIC, *An Examination of the Banking Crises of the 1980s and Early 1990s*, at 119 (1997), available at [https://www.fdic.gov/bank/historical/history/87\\_136.pdf](https://www.fdic.gov/bank/historical/history/87_136.pdf).

<sup>24</sup> H.R. Rep. No. 101-222, at 404 (1989).

Respectfully submitted,

/s/ George F. Verschelden

George F. Verschelden MO Bar # 55128

STINSON LEONARD STREET LLP

1201 Walnut St., Suite 2900

Kansas City, Missouri 64106

Tel: (816) 842-8600

Fax: (816) 691-3495

george.verschelden@stinsonleonard.com

ATTORNEY FOR THE AMERICAN BANKERS  
ASSOCIATION AND THE MISSOURI BANKERS  
ASSOCIATION

### **CERTIFICATE OF SERVICE**

The undersigned attorney hereby certifies that on this 1<sup>ST</sup> day of May, 2017, the foregoing document was filed with the Clerk of the Court by using the CM/ECF system, which sent notification of such filing to all counsel of record.

/s/ George F. Verschelden

Attorney for the American Bankers Association and  
the Missouri Bankers Association