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ATTORNEY GENERAL OPINION NO. 83-26

Marvin S. Steinert
Savings and Loan Commissioner
Room 220
503 Kansas Avenue
Topeka, Kansas 66603

Re: Corporations -- Savings and Loan Associations -- Preemption of State Code by Federal Law

Synopsis: Where there is an impairment of capital of a state-chartered savings and loan association, and such association has been approved as a qualified institution under the Garn-St. Germain Depository Institutions Act of 1982 (P.L. 97-320), section 202 of that act preempts the application of those provisions of K.S.A. 17-5412 and 17-5811 which effectively require the cessation of such association's operations. Moreover, if such association's participation in the programs under the federal act as a qualified institution prevents the state savings and loan commissioner from making a finding that the association's impairment of capital threatens loss to its members, the commissioner has no authority to appoint a trustee for such association on the basis of its impairment of capital. Cited herein: K.S.A. 17-5101, 17-5412, 17-5614, 17-5615, 17-5616, 17-5618, 17-5620, 17-5811, 17-5814, 12 U.S.C. §1729, P.L. 97-320, §202, U.S. Const., Art. VI, cl. 2.

* * *

Dear Commissioner Steinert:

You have requested our opinion regarding the effect of the Garn-St. Germain Depository Institutions Act of 1982 (P.L. 97-320) on certain provisions of the Kansas Savings and Loan Code. The federal statute prompting your inquiry is section

202 of P.L. 97-320 (hereinafter sometimes referred to as "Act"), which amends section 406(f) of the National Housing Act [12 U.S.C. §1729(f) (1980)]. Its intended purpose is to buoy the savings and loan industry and to provide the various savings and loan institutions with time to work out their problems, while taking advantage of their new powers under the Act. (1982 U.S. Code, Cong. & Ad. News, 3063-3066.) Section 202 allows the Federal Savings and Loan Insurance Corporation (FSLIC) to make periodic purchases of capital instruments, known as "net worth certificates," from savings and loan associations that fulfill the requirements of a "qualified institution." The provisions of this section relevant to your inquiry are contained in subsection (a) thereof, as follows:

> "(5)(A)(i) Notwithstanding any other provision of State or Federal law, and without limitation on any authority provided elsewhere in this Act or the Home Owners' Loan Act of 1933, the Corporation [FSLIC], in its sole discretion and on such terms and conditions as it may prescribe, is authorized to increase or maintain the capital of a qualified institution by making periodic purchases of capital instruments to be known as net worth certificates, as defined by the Corporation, for such form of consideration as the Corporation may determine, from such qualified institution, and may authorize such institution to issue such net worth certificates, pursuant to this paragraph.
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> . . . .
>
> "(B) For the purposes of this paragraph, the term 'qualified institution' means an institution the deposits of which are insured under this title or insured or guaranteed under State law which, as determined by the Corporation --
>
> "(i) has net worth equal to or less than 3 per centum of its assets . . . ." (Emphasis added.)

Since all state-chartered savings and loan associations in Kansas are insured by the FSLIC, the provisions of section 202 have potential application to any such association which meets the other definitional requirements of a "qualified institution." Here, it should be noted that section 202 also includes requirements for a qualified institution in addition to that contained in paragraph (B)(i) quoted above. Said requirements are set forth in subparagraphs (ii) through (vi), but only the provisions of subparagraph (i) quoted above have apparent relevance to your inquiry.

Section 202(a) also contains preemptory language, which states:

> "(H) The provisions of the constitution or the laws, civil or criminal, of any State, express or implied, limiting the authority of a qualified institution (i) to take part in programs under this paragraph, (ii) to issue and otherwise deal in net worth certificates issued pursuant to this paragraph, or (iii) to continue operations, including the receipt of deposits and the payment or crediting of interest or dividends to depositors, because of the level of such institution's net worth, surplus fund, or guaranty fund, shall not apply to any qualified institution which the Corporation has approved for the purpose of taking part in programs under this paragraph, continuing operations, or paying interest or dividends." (Emphasis added.)

Here, it is appropriate to note congressional intent in this regard:

> "The bill provides for state law overrides in two areas. One provision ensures that the capital notes issued will be treated as net worth and state chartered institutions will be able to continue to operate and pay dividends." 1982 U.S. Code, Cong. & Ad. News, p. 3064.

In our judgment, such intent is adequately manifested by the preemptory provisions of section 202 of the Act, quoted above, and in light of these provisions, you have inquired whether section 202 of the Act has preempted certain portions of K.S.A. 17-5412 and 17-5811. The former statute states, in part:

> "The board of directors of any association formed under the provisions of this or any previous act may from time to time declare dividends from the earnings of the association to be paid or credited in such manner as may be provided in the bylaws, but no dividends shall be declared except from the earnings and undivided profits of the association: Provided, however, That if the board of directors shall declare, credit or pay any dividend when there is an impairment of capital they shall be jointly and severally liable to the extent of the dividend so declared, credited or paid for all the debts of the association then existing or that shall be thereafter contracted while they shall respectively continue in office." (Emphasis added.)

An "impairment of capital" is defined in K.S.A. 17-5101(k) to mean that "net worth accounts in the aggregate of the association do not exceed 2 1/2% of withdrawable capital."

K.S.A. 17-5811 states:

> "No association shall accept or receive payments upon shares when there is an impairment of capital and any officer, director or employee who shall knowingly violate the provisions of this section or be accessory to or permit or connive at the receiving of accepting payments on such shares, shall be guilty of a felony and upon conviction thereof shall be punished by imprisonment in the penitentiary not less than one (1) year nor more than five (5) years. The word 'share' as used in this section shall not include guarantee shares or stock." (Emphasis added.)

The term "shares" as used in this statute has the same meaning as savings deposits. K.S.A. 17-5814(c).

Therefore, it is clear that the ultimate effect of K.S.A. 17-5412 and 17-5811 is to preclude the further operation of a savings and loan association when there is an impairment of capital of the association. Without the ability to accept deposits or pay interest or dividends, the operations of the association would cease. However, the question for our consideration is whether these statutes, when considered in context with the Act, have the effect of "limiting the authority of a qualified institution . . . to continue operations" and have been preempted by section 202 of the Act.

In addressing this question, we first note the fundamental principle that laws made in pursuance of the United States Constitution are the supreme law of the land. U.S. Const., Art. VI, cl. 2. This is explained by the commentator in 16 Am.Jur.2d Constitutional Law §80, as follows:

> "Since laws enacted in pursuance of the Federal Constitution are given supreme status by the terms of the Constitution itself, it follows that such federal laws control the constitutions and laws of the states, and cannot be controlled by them. State laws are always subordinate, and federal laws, enacted pursuant to the Constitution, are always paramount; hence, a state law is void if contrary to a valid act of Congress. And Congress may, with the support of the supremacy clause, declare state regulations inapplicable to federal

> government activity. In resolving a contention that a particular state statute is invalid under the supremacy clause of the Federal Constitution as conflicting with a federal statute, the controlling principle is whether the state statute interferes with and frustrates the federal statute, and not merely whether the state statute is designed for some conceivable state purpose. In other words, the existence vel non of a conflict depends on the effect of the state statute and cannot be determined merely by a consideration of its purpose." (Footnotes omitted.) (Emphasis added.)

In Maryland v. Louisiana, 451 U.S. 725, 101 S.Ct. 2114, 68 L.Ed.2d 576 (1981), the United States Supreme Court addressed the issue of whether a state could tax the "first use" of certain natural gas brought into the state. The Court held the first use tax violated the supremacy clause because it interfered with federal regulations of the transportation and sale of natural gas. The Court relied on precedent and stated:

> "Of course, a state statute is void to the extent it conflicts with a federal statute--if, for example, 'compliance with both federal and state regulations is a physical impossibility,' Florida Lime and Avocado Growers, Inc. v. Paul, 373 US 132, 142-143, 10 L.Ed.2d 248, 83 SCt 1210 (1963), or where the law 'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.' Hines v. Davidowitz, . . . [312 U.S. 52, at 67]." Id. at 747.

Thus, in the absence of any question that the Act is a validly enacted law, in pursuance of the authority vested in Congress by the U.S. Constitution, we must focus our consideration on whether either K.S.A. 17-5412 or 17-5811 "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." Maryland v. Louisiana, supra.

As previously noted, the Kansas Savings and Loan Code defines impairment of capital as meaning that the net worth accounts in the aggregate of an association do not exceed 2 1/2% of withdrawable capital. K.S.A. 17-5101(k). However, as a threshold for qualifying for the net worth certificate program, section 202 of the Act requires a net worth equal to or less than 3% of the association's assets. Because of the different bases for determining the application of the respective statutes, a comparison for the purposes of determining a conflict in their concurrent application is difficult, and it may be possible that, under some circumstances, the federal act may

be applied without affecting the state statutes. However, we believe it unnecessary to speculate as to such possiblity. Rather, it is only necessary to consider the effect of these statutes when they do, in fact, have concurrent application, i.e., when a state-chartered association meets the Act's requirements for a qualified institution and, at the same time, there is an impairment of such association's capital. Under such circumstances, we believe the questioned provisions of K.S.A. 17-5412 and 17-5811 must yield to the preemptive provisions of the Act.

As we previously noted, when an impairment of a state-chartered savings and loan association's capital exists under Kansas law, state statutes preclude officers and directors from accepting deposits (K.S.A. 17-5811), and prohibit officers and directors from paying dividends or interest on shares or accounts without incurring liability (K.S.A. 17-5412). These statutes, therefore, effectively result in a cessation of such association's operations. Accordingly, where such association has been approved as a qualified institution under the Act, the Kansas statutes would operate in direct conflict with the Act, which is intended to provide for the continued operation of qualified institutions. Thus, in light of this conflict and the principles announced in Maryland v. Louisiana, supra, it is our opinion that the federal law is supreme, preempting the operation of K.S.A. 17-5412 and 17-5811.

You also have inquired whether section 202 of the Act preempts Kansas statutes permitting the state's savings and loan commissioner to appoint a trustee, to take charge of the association, if the commissioner finds "that an impairment of capital exists to such an extent that it threatens loss to the members." K.S.A. 17-5614. The powers of a trustee and the operation of an association in charge of a trustee are addressed in K.S.A. 17-5615 to K.S.A. 17-5618, inclusive. The first of this series of statutes provides, as follows:

> "Any trustee appointed by the commissioner shall have all the rights powers and privileges possessed by the officers, board of directors and members of the association."

However, the trustee's powers are limited by K.S.A. 17-5616, which states:

> "The trustee shall not retain special counsel or other experts, incur any expenses other than normal operating expenses, or liquidate assets except in the ordinary course of operations without written approval of the commissioner."

Further, the operation of an association in charge of a trustee is addressed in K.S.A. 17-5618, which states:

> "While the association is in charge of a trustee, members of such association shall continue to make payments to the association in accordance with the terms and conditions of their contracts, and the trustee, in his discretion, may permit shareholders to repurchase their shares from the association pursuant to the provisions on this act, or under, and subject to, such rules and regulations as the commissioner may prescribe. The trustee shall have power to accept payments upon such shares and such payments when received by the trustee may be segregated if the commissioner shall so order in writing; if so ordered, such payments shall not be subject to offset, and shall not be used to liquidate any indebtedness of such association existing at the time the trustee was appointed for it or any subsequent indebtedness incurred for the purpose of liquidating the indebtedness of any such association existing at the time such trustee was appointed. All expenses of the association including salary and expenses of the trustee during such trusteeship shall be paid by the association."

Finally, K.S.A. 17-5620 requires the commissioner to determine within twelve months whether to restore the management of the association to its board of directors.

Again, in this instance, to determine whether the operation of the foregoing state statutes have been preempted by section 202 of the federal act, it is necessary to determine whether state laws interfere with the objectives of Congress or whether compliance with both federal and state law is a physical impossibility.

Clearly, the authority given to a trustee under Kansas statutes does not prohibit the continued operation of an association when its capital is impaired. To the contrary, the sections of the Savings and Loan Code quoted and discussed above evidence a clear legislative intent that the purpose for the appointment of a trustee is to continue the association's operations under the trustee's direction and supervision. The association may still accept deposits, pay interest or dividends and incur normal operating expenses. It may be argued, therefore, that these statutes do not conflict with the congressional objectives underlying section 202 of the Act and are not preempted thereby.

On the other hand, these statutes also clearly indicate that the operations of an association under the management of a trustee are curtailed to some extent. There are limitations on the trustee's authority (see, e.g., K.S.A. 17-5616) and the operation of the association itself may be limited if the commissioner deems it necessary and appropriate (see, e.g., the provisions of K.S.A. 17-5618 regarding segregation of deposits). Hence, it may be argued that these are statutes which limit the operation of a qualified institution, thereby falling squarely within the purview of the preemptive provisions of section 202, overriding any state law "limiting the authority of a qualified institution . . . to continue operations."

We think it unnecessary to resolve this issue here, in light of our conversations with you subsequent to your request. From these conversations, it is apparent that your principal concern is whether section 202 alleviates the need for the appointment of a trustee when there is an impairment of capital of an association. In our judgment, if such an association is approved as a qualified institution under the Act, the basis for appointing a trustee by the commissioner may not exist. Again, we note that K.S.A. 17-5614 provides as a condition precedent to such appointment a finding by the commissioner "that an impairment of capital exists to such an extent that it threatens loss to the members." (Emphasis added.) Obviously, if the commissioner cannot make such finding as a result of the association being approved as a qualified institution and participating under the Act, the authority for appointing a trustee on the basis of an association's impairment of capital does not exist.

However, we reiterate that our conclusion is predicated on the association being approved as a qualified institution under the Act. The preemptive provisions of section 202 are applicable only to state laws limiting the operational authority of a "qualified institution which the corporation [FSLIC] has approved for the purpose of taking part in programs" under that section.

Very truly yours,

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