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Recent Developments: *Ideal Fed. Save Bank v. Murphy*: Federal Interpretation of the Charter Form Provision for Federally Chartered Mutual Savings Associations Preempts Any State Policy to the Contrary

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***Ideal Fed. Sav. Bank
v. Murphy:***

***FEDERAL
INTERPRETATION
OF THE CHARTER
FORM PROVISION
FOR FEDERALLY
CHARTERED
MUTUAL SAVINGS
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In an unanimous decision, the Court of Appeals of Maryland in *Ideal Federal Savings Bank v. Murphy*, 339 Md. 446, 663 A.2d 1272 (1995), held that where federally chartered mutual savings associations adopt a federal charter form provision that permits "negative voting" for directors, the federal interpretation of the charter form preempts any state policy to the contrary. The court stressed that Maryland state courts must give proper deference to the Office of Thrift Supervision's ("OTS") interpretation of its form charter provisions. In so holding, the court acknowledged that by voting negatively, members of federally chartered savings associations may reject persons whom they do not want controlling and operating an association, even when candidates run unopposed.

Originally chartered as a state savings institution, Ideal Federal Savings Bank ("Ideal") obtained federal insurance and a federal charter following the aftermath of Maryland's savings and loan crisis. Ideal adopted its charter and bylaws from the form for charters and bylaws for federal mutual savings associations found in Title 12, section 544.1 of the Code of Federal Regulations. After "re-chartering" under federal law, Ideal's members nominated ten candidates to fill fifteen available positions for director. Ideal's new federal charter provided for a board of between five and fifteen directors, which its

bylaws set at fifteen. According to both Ideal's federal charter and its bylaws, members were to vote by written ballot either "for," "against," or "abstain" for each director candidate. At Ideal's first board election as a federal institution, members voted in majority for six of the ten nominees, all of whom the acting chair declared elected directors.

Following the election, the four defeated candidates, including Madeline Murphy ("Respondents"), filed suit against Ideal in the Circuit Court for Baltimore City seeking a declaratory judgment that Ideal's members duly elected them to the board of directors. On January 17, 1990, respondents filed a motion for summary judgment and a motion to enjoin Ideal's third scheduled annual meeting and board of directors election. The trial court found that the method of voting for directors employed by Ideal at the 1988 meeting was proper and resulted in the election of only six directors. Finding that the use of negative voting violated Maryland's public policy expressed in section 2-404 of the Maryland Code, Corporations and Associations Article, the Court of Special Appeals of Maryland reversed, stating that the 1988 meeting was invalid and that all the nominees were duly elected.

The Court of Appeals of Maryland granted certiorari to address the issue of whether an election of directors for a federally chartered savings in-

stitution where members may vote "against" each candidate violated Maryland public policy. On appeal, Ideal argued that the court of special appeals misinterpreted the meaning of the term "plurality" and that plurality voting did not occur at the first board election. Conversely, respondents argued that the use of negative voting was improper and as a result, the negative votes amounted to abstentions. *Id.* at 463, 663 A.2d at 1280.

In an opinion written by Judge Chasanow, the court of appeals began its analysis by commenting that an action by stockholders to approve corporate matters generally requires a majority of a quorum of stockholders. *Id.* at 456, 663 A.2d at 1277. The court reviewed section 2-506 of the Maryland Code, Corporations and Associations Article, which states that corporate matters must receive a majority of all votes cast to meet approval. Next, the court cited the exception in section 2-404(d), which provides that receiving a "plurality" of the votes if a quorum exists will satisfy to elect a corporate director "[u]nless the charter or bylaws . . . provide otherwise." *Id.* Construing the meaning of "plurality," the court accepted the court of special appeals' definition based on Black's Law Dictionary as being "the excess of votes cast for one candidate over those for any other." *Id.* at 458, 663 A.2d at 1278 (quoting *Madeline Murphy et al. v. Ideal Fed. Sav. Bank*, Slip

Op. No. 367 at 8-9).

In its analysis of Ideal's argument that plurality voting only applies where three or more persons or choices appear on a single question, the court emphasized that Ideal's charter provision requiring negative voting would not supersede section 2-404(d) "[u]nless the charter or bylaws . . . provide otherwise." *Id.* Because Ideal's charter existed under federal law, the court explained that "even if section 2-404(d) or its 'policy' might otherwise be deemed applicable, it would be preempted by federal law." *Id.* Moreover, federal law solely governs the internal management of federal savings and loans and preempts state law when it conflicts with OTS regulations or federal common law." *Id.* at 459, 663 A.2d 1278. Therefore, the court noted that because Congress authorized the OTS to charter federal savings institutions and regulate their operations, "for" and "against" voting was allowed.

Next, the court noted that an agency's interpretation of an administrative regulation controls "unless . . . plainly erroneous or inconsistent with the regulation." *Id.* at 461, 663 A.2d 1279 (quoting *Bowles v. Seminole Rock & Sand Co.*, 325 U.S. 410, 414 (1975)). On behalf of Ideal, the OTS interpreted Ideal's federal charter as covering elections of directors and all other matters requiring a vote of the members of an association. *Id.* The OTS argued that Ideal's charter, a word-for-word adoption of the Code of

Federal Regulations, required a majority approval to elect a director. *Id.* Because Ideal's charter provided for a board between five and fifteen directors, Ideal and the OTS thus understood that the board election could yield fewer than fifteen directors. *Id.* at 462, 663 A.2d at 1279. Therefore, the OTS interpreted that the majority election of only six directors was in accord with Ideal's charter and federal regulations. In addition, the OTS recognized the federal law assumption that majority votes sometimes leave vacancies on the board of directors. *Id.*

Considering that the OTS drafted the charter form provision and regulated Ideal's operations, the court was persuaded by the federal agency's interpretation of Ideal's federal charter. *Id.* at 462, 663 A.2d 1280. Consequently, the court held that a federal agency's interpretation of a federal charter form provision adopted by a federal institution preempts any conflicting state policy. *Id.* Applying this standard, the court would preempt Maryland public policy if section 2-404(d) advanced a public policy favoring plurality elections without a clear charter or bylaw provision to the contrary. *Id.* As a result, the court concluded that only a majority vote, not a plurality vote, was necessary to elect a director of a federally chartered bank. *Id.*

With respect to respondents' argument that negative voting was improper, the

court emphasized that the OTS permitted negative voting in accordance with Ideal's charter. *Id.* The court first considered respondents' assertion that where positions exceed candidates, any candidate who receives a "for" vote obtains a majority of the votes cast. *Id.* (citing *Coleman v. Marzullo*, 296 So.2d 437, cert. denied, 297 So.2d 206 (La. 1974)). Because the articles of incorporation provided for a majority election, the *Marzullo* court held that where the shareholders nominated only fifteen of twenty possible director candidates, "the stockholder receiving the majority of votes cast . . . receives one vote or more." *Id.* at 464, 663 A.2d 1281 (quoting *Marzullo*, 296 So. 2d at 440).

The court distinguished *Marzullo* in that not one candi-

date opposed another's candidacy, whereas in *Ideal's* election at least two slates partially opposed each other. *Id.* The court further distinguished *Marzullo* from *Ideal* because the *Marzullo* chairman incorrectly classified an abstention as a vote against a candidate. *Id.* Above all, the court reiterated that *Ideal's* charter and the Code of Federal Regulations requires nominees to receive a majority of the votes cast to warrant election. *Id.* As a result, the court found that *Ideal* properly tabulated the negative votes cast at the January meeting and duly elected six directors. *Id.*

By holding that the federal interpretation of the charter form preempted any opposing state policy where a federally chartered mutual savings

association adopted a federal charter form provision, the Court of Appeals of Maryland in *Ideal Federal Savings Bank v. Murphy* articulated the importance of protecting the rights of members of federally chartered savings institutions from state interference. In its basic form, the decision in *Ideal* prohibited a plurality vote for directors and allowed "negative voting." However, *Ideal* derives its true impact from ensuring that the rights of federal savings association members not vary according to local laws or policies. Therefore, the *Ideal* court makes it nearly impossible for federal savings institutions in Maryland to hold plurality elections unless their federal charter clearly states otherwise.

-Mark L. Renbaum

The Court of Appeals of Maryland, the highest tribunal in the State, was created by the Constitution of 1776. The court has sat exclusively in Annapolis since 1851.

