

3942.

## FRATERNAL INSURANCE COMPANY—MAY INVEST IN STOCK OF ANOTHER INSURANCE COMPANY WHEN.

*SYLLABUS:*

*Power of fraternal benefit societies to invest in corporate stock include power to invest in the stock of another insurance company.*

COLUMBUS, OHIO, January 12, 1932.

HON. CHARLES T. WARNER, *Superintendent of Insurance, Columbus, Ohio.*

DEAR SIR:—This will acknowledge receipt of your recent communication, which reads as follows:

“Does a fraternal insurance company have authority under the law to purchase stock in another insurance company?”

The foregoing is, of course, the abstract proposition. The immediate question before the department is whether the ..... Insurance Union, the fraternal, may purchase stock in the ..... Insurance Union, Inc. Of course, as you know, these two companies are intimately related, and in fact so much so under the trust agreement entered into between the two that while they are single entities, yet their interest and object is the same.

I would appreciate an early reply.”

I assume your inquiry has reference to the powers of domestic fraternal benefit societies to invest in corporate stock, including the stock of insurance companies.

Section 9472, General Code, regulates the collection of assessments by fraternal benefit societies and the purposes for which the proceeds may be used. Section 9472, General Code, provides:

“Every provision of the laws of the society for payment by members of such society, in whatever form made, shall distinctly state the purpose of the same and the proportion thereof which may be used for expenses, and no part of the money collected for mortuary or disability purposes or the net accretions of either or any of such funds shall be used for expenses.”

It is contemplated that the funds of a fraternal benefit society will generally be used for three purposes: (1) to pay disability claims, (2) to pay death claims, and (3) to pay operating expenses of the association. It is foreign to the purpose of such associations to speculate in stocks or to purchase stock for the purpose of obtaining control of other corporations, whether they be insurance companies or engaged in any other business. No statutory authority for such operations can be found, either express or implied. The legislature has provided for the investment of idle funds of fraternal benefit societies. Sections 9471, 9357, General Code.

Section 9471, General Code, provides:

“Every society shall invest its funds only in securities permitted by

the laws of this state for the investment of the assets of life insurance companies; provided, that any foreign society permitted or seeking to do business in this state, which invests its funds in accordance with the laws of the state in which it is incorporated, shall be held to meet the requirements of this act for the investment of funds."

Section 9357 of the General Code, as amended in 114 O. L., p. 131, governs the investments of life insurance companies and therefore the investments of fraternal benefit societies. So far as applicable to your question, section 9357, General Code, provides as follows:

"The capital, surplus and all accumulations of every domestic life insurance company shall be invested as follows:

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J. (a) In the preferred stocks of any company organized under the laws of the United States, and/or of one of the several states, upon which the net earnings each year for a period of not less than seven fiscal years preceding purchase thereof, after deduction of interest on all mortgages, bonds, debentures and funded debts and proper charges for replacements, depreciation and obsolescence, shall have averaged at least four times the amount which may be required to pay the dividends on such preferred stocks, and in which the mortgages, bonds, debentures, funded debts and preferred stocks shall not in the aggregate exceed sixty per cent of the total of the capitalization of such company, including mortgages, bonds, debentures, funded debts and preferred and common stocks.

(b) A domestic life insurance company shall not purchase any preferred stocks at a time when the total market values of such stocks then owned with those purchased shall exceed in the aggregate of book values and purchase price the capital surplus and contingency funds (excluding all reserves required by law) of such company on the 31st day of December preceding the date of such purchase, or contemplated purchase, provided that in case of appreciations in values of stocks owned the cost rather than the market values shall be used in arriving at such aggregate; the purpose hereof being to restrict the investments of such company in all stocks to capital, surplus and contingency funds.

(c) No domestic life insurance company shall at any time invest more than five per cent of its capital, surplus and contingency funds as of December 31st preceding date of purchase in the bonds and/or preferred stocks of a particular corporation, nor shall it at any time own more than five per cent of the outstanding stocks and bonds of any corporation.

K. In loans for periods not exceeding one year upon the pledge of any securities in which such domestic companies are authorized by this act to invest; provided, however, that any loan upon such a pledge shall not exceed eighty per cent of the cash market value of the collateral at the time of the making of such loan, nor shall any company through the collateral pledged to it exceed the amounts which such company may, under the provisions of this act, invest in one corporation so that, in the stocks and securities which may be owned and those which

are pledged to it, the limitations in this act prescribed might be indirectly evaded.

L. No domestic life insurance company shall subscribe to or participate in any underwriting for the purchase or sale of securities or property, nor shall it enter into any transaction for such purchase or sale on account of said company jointly with any other person, nor shall any such company enter into any agreement to withhold from sale any of its property, but the disposition of its property shall be at all times within the control of its board of directors.

M. (a) In the determination of capitalization in the foregoing paragraphs of this act the value of all bonds, debentures and funded debts, and non-convertible or non-participating preferred stocks, shall be figured at par. Participating or convertible preferred shares shall be figured at par or market on December 31 immediately preceding, whichever is higher, and the value of all common shares shall be figured at the market on December 31 immediately preceding.

(b) The term 'funded debt' shall mean all interest bearing obligations maturing in more than one year from their issuance and all guaranteed or assumed interest bearing obligations or stock. Securities or stock of such corporation pledged to secure other funded debt of the corporation shall not be included in the term 'funded debt.'

N. No domestic life insurance company shall be permitted to invest in or loan upon its own stock, either directly or indirectly.

O. If the investments of any domestic life insurance company shall at the time of the making thereof be otherwise than as authorized in this act, such investments shall not be admitted or accepted as legal or authorized investments for such company.

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As disclosed in section 9357, General Code, the conditions and restrictions relative to the investment by a fraternal benefit society in stocks of any corporation are that:

1. A fraternal benefit society may not invest its funds in any event in common stock but only in such stocks as are legally classified as preferred. You do not state whether or not the stock which is proposed to be purchased would be classified as preferred stock, and I am therefore unable to state whether it satisfies this condition of the statute.

2. Any corporation, in whose preferred stock a fraternal benefit society proposes to invest, must show average annual net earnings, after deduction of the corporate liabilities defined by section 9357, subsection J, clause (a), General Code, for seven fiscal years prior to the date of the proposed purchase, of at least four times the dividends payable on such preferred stock.

3. Any corporation, in whose preferred stock a fraternal benefit society proposes to invest, must not have outstanding mortgages, bonds, debentures, funded debts and preferred stocks in excess of sixty per cent of its capitalization as defined in section 9357, subsection J, clause (a), General Code.

4. Such fraternal society may not in any event purchase such preferred stocks if the total market value of all the stocks owned by said fraternal benefit

society, together with the stock proposed to be purchased, will exceed in the aggregate of book value and purchase price the equivalent in such society of the capital, surplus and contingency funds (excluding all reserves required by law) of a life insurance company as of the 31st day of December, prior to the date upon which the fraternal benefit society proposes to purchase such corporate stock, subject to the proviso set forth in section 9357, General Code, subsection J, clause (b), supra. In the event the value of the stock has increased over its cost to the society, the cost shall be used in computing the total market values of all stock owned by the society.

5. Section 9357, General Code, subsection J, clause (b), supra, provides: “ \* \* \* the purpose hereof (of section 9357, General Code, supra) being to restrict the investments of such company in all stocks to capital, surplus and contingency funds.” (Parenthetical insertion the writer’s.) A domestic fraternal benefit society’s assets consist of funds and accretions thereto for the payment of claims and expenses which would be included in the terms “surplus and contingency funds,” as used in the above statute. In a technical sense, capital, as used in section 9357, General Code, has application only to domestic life insurance companies. It is clear that if the claims against a fraternal benefit society, which are due and payable, equal or exceed the funds of the society from which such claims may be satisfied, such funds may not be invested.

6. A fraternal benefit society may not invest in excess of five per cent of its funds in bonds or preferred stocks of any one corporation.

7. A fraternal benefit society is not permitted to own more than five per cent of the outstanding stocks and bonds of any one corporation.

8. Under the power to loan on stocks, a fraternal benefit society may not evade the prohibitions relating to its powers to own stocks.

9. Fraternal benefit societies may not subscribe to or engage in any underwriting activity in reference to the purchase or sale of securities, or, more specifically, enter into any transaction which will remove the power to control and dispose of its property from its board of directors.

Although not in terms applicable to fraternal benefit societies, you will note the prohibition contained in section 9357, General Code, subsection (n), prohibiting a life insurance company from investing in or loaning upon its own stock, directly or indirectly. Since the two corporations which you mention in your communication are, in fact, separate entities, in the absence of further facts, I do not feel that the provision of section 9357, General Code, last mentioned is applicable.

I am not unmindful of the provisions of section 9358, General Code, which reads as follows:

“The preceding section (section 9357, General Code) shall not prohibit a company from accepting any other assets than therein enumerated in payment of debts due it, in order to protect its interests, or from acquiring real estate for its own use, or by foreclosure in accordance with the laws of this state, provided that unincumbered real estate as referred to in the preceding section shall be held to mean real estate not subject to any other lien, except taxes or assessments not yet due.” (Parenthetical insertion the writer’s.)

It is doubtful if the term “funds,” used in section 9471, General Code, can

be construed to include the term "debts," as used in section 9358, General Code. I find no other statute in Tit. IX, Div. III, Subsection I, Ch. 4, General Code, relating to fraternal benefit societies which by direct reference, or by plain implication, would make section 9358, General Code, applicable to such societies. Otherwise this statute is inapplicable. Section 9465, General Code.

It is obviously a question of fact and law to be determined upon a consideration of the circumstances surrounding each proposed purchase as to whether a fraternal benefit society is exceeding its powers under the foregoing in the investment of stock in another insurance company. Other than the implied prohibition of section 9357, subsection N, General Code, as applied to fraternal benefit societies, there are no peculiar restrictions as to the investment in stocks of insurance companies which are not equally applicable to investment by such societies in other corporate stocks.

Your communication does not set forth the controlling facts, nor am I otherwise informed thereof sufficiently to pass upon the legality of the specific transaction you have before you. Having these facts before you, the statutes cited and quoted above will, I believe, enable you to determine as to whether the proposed purchase of stock in another insurance company is valid.

It is apparent from an examination of sections 9357 and 9471, General Code, that the legislature intends that the assets of a fraternal benefit society shall be invested with a view to safety rather than to produce large profits or to effectuate other purposes unless either can be concurrently accomplished, however beneficial to the society and its policy holders such other purposes may be. This legislative intent should be paramount consideration in construing and administering these statutes.

Further than pointing out the general rules governing investments in corporate stocks by domestic fraternal benefit societies, as I have attempted to do herein, I feel no more specific answer to your inquiry may be made.

Respectfully,

GILBERT BETTMAN,  
*Attorney General.*

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3943.

APPROVAL, LEASE TO BUILDING, YARD AND OIL HOUSE AT 536  
PARK STREET SOUTH AND FIRST FLOOR OF GARAGE SOUTH  
OF HOSTER STREET, COLUMBUS, OHIO, FOR USE OF THE STATE  
BINDERY DEPARTMENT.

COLUMBUS, OHIO, January 12, 1932.

HON. T. S. BRINDLE, *Superintendent of Public Works, Columbus, Ohio.*

DEAR SIR:—Your immediate predecessor, Albert T. Connor, submitted for my consideration a form of lease in quintuplicate whereby E. G. Buchsieb grants to the State of Ohio, for the use of the State Bindery Department, the entire building, yard and oil house at No. 536 Park Street South, and the first floor of the second garage south of Hoster Street, in the city of Columbus, Ohio, for