UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEW JERSEY
Caption in compliance with D.N.J. LBR 9004-2(c)

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Co-Counsel to Ad Hoc Committee of Holders of 8.5% Senior Secured Notes due 2015

In re: TCI 2 HOLDINGS, LLC, et al.,[1] Debtors.	Chapter 11 Case No. 09-13654 (JHW) (Jointly Administered) **Hearing Date: December 14, 2009 at 2:00 p.m.**

OBJECTION OF THE AD HOC COMMITTEE OF HOLDERS OF 8.5% SENIOR SECURED NOTES DUE 2015 TO AMENDED DISCLOSURE STATEMENT FOR JOINT PLAN OF REORGANIZATION UNDER CHAPTER 11 OF THE BANKRUPTCY CODE PROPOSED BY BEAL BANK (f/k/a BEAL BANK S.S.B.) AND BEAL BANK NEVADA

[1] The Debtors in these Chapter 11 Cases, along with the last four digits of each Debtor's federal tax identification number, are: TCI 2 Holdings, LLC (0526); Trump Entertainment Resorts, Inc. (8402); Trump Entertainment Resorts Holdings, L.P. (8407); Trump Entertainment Resorts Funding, Inc. (8405); Trump Entertainment Resorts Development Company, LLC (2230); Trump Taj Mahal Associates, LLC, d/b/a Trump Taj Mahal Casino Resort (6368); Trump Plaza Associates, LLC, d/b/a Trump Plaza Hotel and Casino (1643); Trump Marina Associates, LLC, d/b/a Trump Marina Hotel Casino (8426); TER Management Co., LLC (0648); and TER Development Co., LLC (0425).

The ad hoc committee (the "Ad Hoc Committee") of holders of certain of the 8.5% Senior Secured Notes due 2015 (the "Second Lien Notes" or "Second Lien Noteholders"), by and through its undersigned counsel, hereby objects to the Amended Disclosure Statement For Joint Plan of Reorganization Under Chapter 11 of the Bankruptcy Code dated December 4, 2009 (the "Beal Disclosure Statement") proposed by Beal Bank (f/k/a Beal Bank S.S.B.) and Beal Bank Nevada (together, "Beal Bank") in respect of the Joint Plan of Reorganization Under Chapter 11 of the Bankruptcy Code dated December 4, 2009 (the "Beal Plan") proposed by Beal Bank; and in support hereof respectfully represents as follows:

PRELIMINARY STATEMENT

1. The Beal Disclosure Statement is palpably inadequate. Although the Beal Plan is radically different than the prior version of the Debtors' plan insofar as it purports to offer creditors an equity investment in a reorganized company controlled by Beal Bank, the Beal Disclosure Statement essentially just reproduces the same disclosure made in the outdated disclosure statement. As a consequence, the Beal Disclosure Statement fails to provide necessary disclosure regarding Beal Bank, in its capacity as the future controlling equity holder of a private company and plan proponent, and the reorganized Debtors' operations—information that was not previously contained in the Debtors' prior disclosure statement.

2. In particular, the Beal Disclosure Statement fails to come forward with *any* explanation as to the potential impact of banking regulations that may preclude Beal Bank or any of its subsidiaries formed under the Beal Plan from moving forward with the such plan. Specifically, Beal Bank and Beal Bank Nevada—a savings and loan association and state chartered bank, respectively—are prohibited from participating in non-banking related activities and may not equitize debt unless appropriate applications are submitted in advance to state and

federal regulators and requisite approvals are obtained. As demonstrated below, Beal Bank must persuade state and federal banking regulators, upon requisite notice, that the equitization of its debt under the Beal Plan is an appropriate exercise of its salvage powers and is ***necessary*** to protect against the loss of its investment. There is no indication in the Beal Disclosure Statement as to how or why the regulators can reasonably be expected to approve Beal Bank's proposal to provide a direct equity investment and fully equitize its debt where Beal Bank acknowledges that it is over-secured. Beal Bank's inability to make the required regulatory showing is especially apparent due to the presence of the viable alternative presented by the Ad Hoc Committee's plan (the "AHC Plan"), which offers Beal Bank a significant cash pay down and new debt. Moreover, Beal Bank will be hard pressed to explain how voluntarily equitizing debt and operating Atlantic City casinos would not place an undue risk upon the banking system in light of the current macroeconomic banking environment and the declining Atlantic City gaming market. The Beal Disclosure Statement simply offers *no* disclosure as to the fatal flaws to the Beal Plan (if not potential violations of applicable non-bankruptcy law). Unless and until Beal Bank can demonstrate to this Court that its plan is feasible from a regulatory perspective and filed in good faith, then the Debtors' estates should not be required to bear the expense and delay associated with what may be a meaningless proposal.

3. Apart from its obligation to demonstrate, as a threshold matter, that its plan has some reasonable basis for moving forward, Beal Bank has similarly failed to provide critical information relating to, among other things: (a) the economic rationale for its plan proposal and creditor recovery levels; (b) significant risks facing Second Lien Noteholders and general unsecured creditors as potential holders of a minority stake in a privately held company controlled by Beal Bank, including the likely possibility that Beal Bank may cause the company

post-emergence to incur indebtedness or engage in other transactions that may be prejudicial to minority shareholders, such as dilutive equity issuances, and the potential impact of such transactions on value; (c) Beal Bank's long term business plan (in fact, any business plan), since Beal Bank can no longer rely on the consensual use of the Trump brand—a key component of Beal Bank's earlier plan and previously described by Beal Bank as ***indispensable*** to the operations of the reorganized Debtors; and (d) the impact of the banking regulatory holding period upon the Debtors' future business, which, under a valid exercise of salvage powers, likely does not exceed, at most, two to five years.

4. Accordingly, the Ad Hoc Committee respectfully submits that Beal Bank should not be permitted to solicit its plan and disclosure statement unless Beal Bank first demonstrates that it is capable of moving forward with its plan, and until it adds critical information demonstrating that Beal Bank can satisfy applicable banking regulations. In order to avoid undue delay, the Court should require that any modifications to be made to the Beal Disclosure Statement should be presented by Beal Bank to creditors and the Court promptly following the hearing to consider the Beal Disclosure Statement.

RELEVANT BACKGROUND

A. The Debtors' Plan

5. On August 3, 2009, the Debtors filed a plan of reorganization sponsored by Beal Bank and Donald Trump (the "Debtors' Plan"), pursuant to which Beal Bank and Donald Trump were given the exclusive right to acquire 100% of the equity of the reorganized Debtors for $100 million. That plan also reinstated the pre-petition balance of Beal Bank's debt at a higher coupon rate (albeit with an extended maturity date of 2020). All other stakeholders, including the claims of holders of $1.25 billion in Second Lien Notes, were wiped out. Central to that

plan, according to Beal Bank, was not only Mr. Trump's financial contribution but the continued use of the Trump brand and the continued participation and services of Donald Trump in the reorganized Debtors' businesses.

6. Faced with the prospect of a zero recovery and what appeared to be a plan that violated the absolute priority rule and paid Beal Bank more than 100% on account of the secured portion of its claim, the Ad Hoc Committee successfully moved to terminate exclusivity and filed a competing plan of reorganization on August 31, 2009.

7. The competing AHC Plan (as subsequently amended on November 5, 2009) contemplated an investment of $225 million in new equity capital in the form of a rights offering backstopped by the Ad Hoc Committee in exchange for a backstop fee payable in the form of 20% of the new common stock of the reorganized Debtors. Holders of the Second Lien Notes, together with general unsecured creditors, would have been entitled to receive (a) 5% of the new common stock, and (b) subscription rights to acquire 75% of the new common stock. General unsecured creditors that were not accredited investors and therefore ineligible to receive subscription rights would be entitled to receive cash in an amount equal to the value of the subscription rights.

8. Under the AHC Plan, Beal Bank would receive a $125 million in cash to pay down from the proceeds of the rights offering, as well as all net cash proceeds from the sale of the Trump Marina Casino to Coastal Marina, LLC as contemplated by the AHC Plan. The remaining balance of the Beal Bank debt would accrue interest at an annual rate equal to the rate proposed by Beal Bank under the Debtors' Plan or such other rate to be determined by the Court sufficient to comply with the cramdown procedures in section 1129(b)(2)(A) of the Bankruptcy

Code. Thus, under the AHC Plan, Beal Bank was assured that it would be paid in full on account of its allowed secured claim.

9. Beal Bank's subsequent attempts to appeal the Court's exclusivity decision and seek a stay of the solicitation of the AHC Plan failed.

10. On November 5, 2009, this Court entered an order authorizing the joint solicitation of the Debtors' Plan and the AHC Plan. Thereafter, the parties engaged in comprehensive discovery in preparation for a dual plan solicitation and confirmation battle at great expense to the Debtors' estates and the Ad Hoc Committee.

B. The Ad Hoc Committee's Settlement With Donald and Ivanka Trump

11. After concluding that the AHC Plan was the better path to emergence, and in an effort to reduce litigation costs that were accruing to the estate at over $1 million a week, Donald and Ivanka Trump agreed to settle all pending disputes with the Ad Hoc Committee. On November 16, 2009, Donald Trump terminated the Purchase Agreement under the Debtors' Plan and entered into a settlement agreement with the Ad Hoc Committee. Under the terms of that agreement, in exchange for 5% of the New Common Stock, warrants to acquire up to an additional 5% of the New Common Stock and releases, Mr. Trump agreed to support the AHC Plan and to enter into a trademark license agreement and services agreement with the reorganized Debtors for the continued use of the Trump brand as well as a non-compete provision that prohibits Donald Trump from competing against the Debtors within its regional market. On November 24, 2009, the Ad Hoc Committee filed an amended version of the AHC Plan, incorporating the settlement with Donald and Ivanka Trump.

12. At a hearing held before this Court on December 3, 2009, the Debtors announced that, after careful consideration of the AHC Plan and the plan proposal made by Beal Bank, its Board of Directors had decided to support the AHC Plan. The AHC Plan is in the process of

being amended to provide for the Debtors to be a co-proponent, and will be filed with this Court shortly.

C. Beal Bank's Foreclosure-Like Proposal

13. In what is, in substance, a foreclosure upon the Debtors' assets for its primary benefit, Beal Bank has proposed the following restructuring terms:

- Beal Bank's proposal contemplates a $225 million rights offering backstopped by Beal Bank, pursuant to which Second Lien Noteholders and general unsecured creditors will be entitled to purchase up to 32.5% of the common stock in the reorganized Debtors;
- The reorganized Debtors would be a private, non-reporting company; the new common stock would not be registered and would be subject to substantial transfer restriction;
- $100 million of the rights offering proceeds would be recycled and used to pay down Beal Bank;
- No longer concerned with salvaging its loan, Beal Bank now seeks to fully equitize the remaining balance of its debt on a voluntary basis, without regard to potential regulatory infractions, and purports to characterize 10% of that equity as a backstop fee;
- In the event of 50% or more participation in the rights offering (which is an impossibility because the Ad Hoc Committee comprises more than 60% of the Second Lien Notes and will not accept the Beal Plan), Second Lien Noteholders and general unsecured creditors would be entitled to a primary distribution of 2% of the new common stock. Otherwise, in lieu of the equity, Second Lien Noteholders and general unsecured creditors will be entitled to share in a fixed pool of $13.9 million in cash; and
- Beal Bank (or its designee) will be entitled to receive the sole share of preferred stock to be issued by NewCo giving it control over significant corporate transactions.

14. Despite repeatedly proclaiming that it was undersecured and the only party with an economic stake in the outcome of these cases, Beal Bank now adopts the Ad Hoc Committee's total enterprise value (the "TEV") midpoint of $499 million, thereby

acknowledging that past recriminations about irreparable harm or loss to collateral value were nothing more than bombast rhetoric.

I.

BEAL BANK IS INCAPABLE OF MOVING FORWARD WITH ITS OWN PLAN

15. As a threshold matter, and before the Debtors' estates bear the expense and delay associated with the solicitation of the Beal Plan, Beal Bank must, at a minimum, demonstrate to creditors and this Court that it is not prohibited by non-bankruptcy law from moving forward with the Beal Plan. Here, Beal Bank may be incapable of consummating the Beal Plan due to banking regulatory constraints that are not disclosed in the Beal Disclosure Statement; Beal Bank's failure to comply with these regulations would result in patent violations of the Bankruptcy Code were Beal Bank authorized to commence solicitation.

16. The extent of the lack of disclosure of these regulatory issues is extraordinary. In its disclosure statement, Beal Bank makes only an oblique reference to the potential regulatory risks facing Beal Bank under its plan: "Beal Bank believes that, other than casino approval, there are no regulatory issues that could adversely affect the Plan." Beal Disclosure Statement at III.B. However, Beal Bank and Beal Bank Nevada, each of which hold first lien debt claims against the Debtors' estates, are heavily regulated banks that cannot equitize debt unless narrow conditions are met, notice procedures are complied with and applicable banking regulatory approvals are obtained. Yet no mention of any kind is made with respect to the nature of those regulations, the basis for Beal Bank's belief that it is or will be in compliance with those regulations, or the potentially fatal risks to the Beal Plan if it is not. Unless Beal Bank can demonstrate that is plan constitutes an appropriate use of its salvage power, it cannot, by law, move forward with the Beal Plan.

17. The pertinent regulatory constraints are summarized below. Upon information and belief, Beal Bank (f/k/a Beal Bank S.S.B.), headquartered in Texas, is a federally chartered savings and loan whose operations are regulated by a federal agency, the United States Office of Thrift Supervision ("OTS"). The OTS has expressly ruled that a federal thrift may acquire equity securities in exchange for a debt previously contracted in good faith ("DPC debt") solely to the extent necessary to "salvage" its loan. *See* Memorandum dated Jan. 27, 2988 (1988 WL 1021862 O.T.S.), a copy of which is annexed in Annex A hereto. Specifically, the OTS has opined that:

> [T]he acquisition of the stock of a borrower, in lieu of foreclosure, should be deemed to be part of a bona fide salvage operation if and when circumstances at the time of the acquisition are such that a reasonable business person could conclude that acquisition of the borrower's stock is the best way for the association to minimize or avoid loss on its loan. Whether this standard is met in each particular case is, of course, a matter for the determination of the SA [i.e., the regional office of the OTS]. It should be stressed, however, that the question to be decided by the SA is not whether the SA believes that acquisition of the stock of the borrower is the best solution to the problem, but whether the SA believes that a reasonable business person could so conclude. The fact that the acquisition of stock may result in an even greater loss to the association if the salvage scheme fails is not, of itself, a presumptive disqualifier, provided there is a reasonable prospect that the association's prospective loss on its investment will be reduced if the salvage scheme succeeds.

Id. (citations omitted); *see also Atherton v. Anderson*, 86 F.2d 518, 525 (6th Cir. 1936), *rev'd on other grounds,* 302 U.S. 643 (1937); *Eureka Building & Loan Assoc'n v. Greenwood Hotel Corp.*, 103 P.2d 46, 46 (Kan. 1940).

18. To the extent that Beal Bank validly exercises its salvage power and elects to hold the assets so acquired in a subsidiary, as opposed to holding those assets directly, then additional

notice and approval requirements apply. *See* 12 CFR § 559.13 (2009).[2] Specifically, under 12 CFR § 559.13, Beal Bank would be required to give 30 days' advance notice to OTS if certain criteria are met. In addition, Beal Bank would need to file a prior application with the Federal Deposit Insurance Corporation ("FDIC") pursuant to 12 CFR § 362.15. *See* 12 CFR § 362.15 (2009).[3]

19. Upon information and belief, Beal Bank of Nevada is a Nevada state-chartered non-member bank whose operations are regulated by the State of Nevada Banking Commission and the FDIC. As such, the salvage powers of the bank, to the extent that the bank is planning to acquire equity securities in exchange for DPC debt, are governed by Nevada state law. Specifically, Nevada Revised Statutes ("NRS") 662.135.4 ("Limitations on investment in stock of or membership in other banks and business organizations") provides that "[a] bank shall not invest in the stocks or ownership of other corporations, firms, partnerships or companies except as otherwise provided in this title, unless the investment is made to protect the bank from loss." 2008 Nev. Stat. 662.135. In other words, similar to a national bank, a Nevada chartered bank can not invest in companies engaged in "nonbanking activities" unless the investment is made to protect the bank from loss. The NRS does not define "loss" or prescribe the criteria by which a Nevada state bank may exercise its salvage power exception.

20. If Beal Bank Nevada intends to hold the securities in a subsidiary, the bank may be subject to 12 CFR § 362.4. *See* 12 CFR § 362.4 (2009).[4]

21. In addition, to the extent that Beal Bank or Beal Bank Nevada validly exercise their salvage powers, assets acquired pursuant thereto may be subject to a maximum holding

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[2] A copy of 12 CFR § 559.13 is annexed in Annex A hereto.

[3] A copy of 12 CFR § 362.15 is annexed in Annex A hereto.

[4] A copy of 12 CFR § 362.4 is annexed in Annex A hereto.

period within which the assets must be sold. In particular, Beal Bank would likely be subject to a five-year holding period, whereas Beal Bank Nevada would likely be subject to a two-year holding period.[5]

22. Here, there is no indication or disclosure of any kind in the Beal Disclosure Statement that Beal Bank has sought the approval of the regional office of the OTS or the State of Nevada Banking Commission in anticipation of acquiring stock in exchange for DPC debt. To the extent Beal Bank and Beal Bank Nevada intend to acquire stock through a subsidiary, there is no indication that approval has been sought from either the OTS or the FDIC. Such omissions are particularly significant in light of the fact that Beal Bank estimates that its plan may go effective as early as January 2010. *See* Beal Disclosure Statement at III.B. ("Beal Bank anticipates that the Effective Date will occur in January 2010. However, a January, 2010 Effective Date may be delayed due to litigation relating to the Beal Bank's Plan, the AHC Plan and/or any delays in the receipt of approvals from the NJ CCC."). No mention is made of the

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[5] The applicable holding period for national banks is five years, subject to extension with regulatory approval. *See* Interpretive Letter No. 1007, 2004 WL 2191294 (O.C.C. September 7, 2004), a copy of which is contained in Annex A attached hereto. The United States Comptroller of the Currency ("OCC"), the regulator of national banks, when approving equity for debt swaps in the exercise of salvage powers by national banks, noted that there was no statutory provision governing the holding period for such equity. *Id.* However, the OCC noted there was a statute that imposed a five-year holding period for foreclosed property. *Id.* The OCC reasoned that an equity for debt swap is analogous to a foreclosure so the five-year holding period would be applied to such equity. *Id.* The Nevada structure is similar in that the law does impose a two-year statutory holding period (subject to extension with regulatory approval) for non-real estate acquired in a foreclosure, but Nevada law does not address a holding period for assets acquired in a salvage situation. In an effort to maintain parity among state and federal charters, state banking commissioners often look to published precedents from the OCC for guidance in areas where state law is silent. In various rulings issued by the OCC in connection with the exercise by a national bank of its salvage powers, the OCC has ruled that the holding period for nonconforming (i.e., nonbanking) assets acquired under the exercise of a bank's salvage powers (e.g., a DPC debt for equity swap) will be the same as the holding period as for assets acquired in foreclosure. *Id.* If Nevada were to adopt this approach, then the Nevada Banking Commissioner would likely look to the language of NRS 662.125.4, the Nevada counterpart to the national bank "foreclosure" rule, when determining the holding period for equity exchanged for DPC debt, which imposes a two-year holding period, unless extended by the Commissioner. In sum, if a Nevada bank were to acquire non-permissible equities in a foreclosure, the equities must be disposed of within two years unless regulatory permission is obtained to extend the holding period. As is the case with national banks, this same two year holding period limit (without regulatory approval) should apply to otherwise non-permissible equities acquired in exchange for DPC debt.

possibility of any delay due to banking regulatory concerns or approvals. Unlike the New Jersey CCC regulatory process, no representation is made that that the necessary applications by Beal Bank have been filed and/or are pending.

23. Moreover, Beal Bank makes no attempt to either distinguish itself from the application of the "salvage power" exception or to demonstrate that it can meet that exception. For example, Beal Bank offers no explanation as to whether its plan is necessary to salvage its pre-petition loan when, as here, (a) Beal Bank has acknowledged that it is over-secured, (b) it previously filed a plan that was continent upon the reinstatement of the full amount of its debt, (c) an alternative and viable plan is currently on the table that offers Beal Bank a significant cash payment and new debt, and (d) the proposal will be considered against the backdrop of a national macroeconomic crisis, the failure at an unprecedented rate of banks in the United States, and a trough gaming market in Atlantic City. Beal Bank is particularly hard pressed to explain how, with state and national banks failing across the country, there will be any appetite by the regulators to allow Beal Bank to fully equitize its debt and operate a gaming casino. No disclosure is made at all as to the application of any banking regulations in the Beal Disclosure Statement.[6]

24. The failure of Beal Bank to demonstrate its compliance with these banking regulations renders the Beal Plan patently unconfirmable as not having been proposed in good faith and not by any means forbidden by law (11 U.S.C. § 1129(a)(3)), not feasible (11 U.S.C. § 1129(a)(11)), and against public policy with respect to the manner of selection of officers and directors under the plan (11 U.S.C. §§ 1129(a)(1), 1129(a)(2), 1123(a)(7)).

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[6] Beal Bank must also be required to demonstrate proof of adequate notice and service of its motion to shorten time, as well as proof of service of the Beal Disclosure Statement and Beal Plan, upon the applicable banking regulators and agencies.

II.

THE BEAL BANK PLAN CONTAINS OTHER INFIRMITIES

25. The Beal Plan also contains other violations of the Bankruptcy Code. The Beal Plan contemplates the issuance of a single share of preferred stock by NewCo, a Delaware corporation to be formed under the Beal Plan, to Beal Bank or a wholly-owned subsidiary thereof. The terms of the preferred stock confer upon Beal Bank veto power with respect to significant corporate transactions. To the extent the preferred stock is deemed a non-voting security for purposes of section 1123(a)(6) of the Bankruptcy Code, then the Beal Plan violates the first clause of section 1123(a)(6). *See* 11 U.S.C. § 1123(a)(6). To the extent the preferred stock constitutes a "voting" security, then Beal Bank fails to demonstrate that the Beal Plan contemplates an appropriate distribution of voting power among several classes of securities issued under the plan, as required under section 1123(a)(6). *Id.*

III.

THE BEAL DISCLOSURE STATEMENT CONTAINS INADEQUATE INFORMATION

A. Description of Regulatory Requirements and Risks

26. As shown above, to the extent the Court is satisfied that Beal Bank may move forward with its disclosure statement, then the Beal Disclosure Statement must include a reasonably detailed description of the pertinent banking regulations, the regulatory notice and approval process, appropriate risk factors and Beal Bank's assessment as to whether it is capable of undertaking the transactions contemplated by the Beal Plan. Beal Bank must also disclose that it may be subject to a holding period, requiring Beal Bank and Beal Bank Nevada to sell their equity stake within two to five years (if not sooner).

B. Economic Rationale for the Beal Plan and Beal's Recovery

27. Without support from any major constituency in this case, Beal Bank has proposed a plan proposal that seemingly lacks any economic rationale from the Second Lien Noteholders' perspective. Significantly, Beal Bank has completely reversed itself and now admits that it is over-secured but offers no justification for the equity splits under its plan proposal, no explanation for Beal Bank's assertions regarding the value of its proposal as compared to the value offered by the AHC Plan, and no basis for, in substance, usurping all of the equity value of the reorganized Debtors.

28. The Beal Plan is tantamount to a foreclosure and lacks the support of any of the main constituencies in these cases. The Ad Hoc Committee, with over 61% of the Second Lien Notes, is committed to the AHC Plan and will not vote to accept any Beal Plan. Moreover, the prospect of acquiring an illiquid minority stake in a privately held gaming company controlled by a regulated bank makes it highly improbable that any other Second Lien Noteholders will consider making an equity investment with Beal Bank. Beal Bank no doubt appreciates these points, but has engineered its proposal in an attempt to persuade the Court that it offers creditors a meaningful investment opportunity. In substance, the Beal Plan is not different from a foreclosure upon the Debtors' assets for the primary benefit of Beal Bank; the prospect of subscription rights to acquire valueless stock is nothing more than window dressing.

29. Beal Bank asserts that it will be recovering "less than 100%." Beal Disclosure Statement at II.B. In fact, as demonstrated below, Beal Bank will be recovering *more* than 100% of its claims—perhaps *substantially* more than 100% if proper effect were given to section 506(b) of the Bankruptcy Code and the recharacterization provisions of the Final Cash Collateral Order entered by the Court on March 23, 2009 [D.I. 157], which would allow the estate to

recharacterize cash payments made to or for the benefit of Beal Bank in excess of its "over-security."

30. The analysis set forth below projects the recovery to Beal Bank based upon the equity value implied under the Beal Plan, and readily demonstrates that Beal Bank will recover more than 100% of its claims:

($ in '000s)	Equity Value
Total Enterprise Value [(1)]	$499,000
Less: Other Secured Claims [(2)]	(6,019)
Less: New First Lien Debt	-
Plus: Proposed Cash Equity Infusion [(3)]	111,063
Implied Equity Value Upon Emergence	**$604,043**

	First Lien Debt Recovery	First Lien Debt Recovery
	No Recharacterization	Recharacterization
First Lien Debt Equity % [(4)]	67.55%	67.55%
Total $ Equity Distribution to First Lien	**$408,019**	**$408,019**
First Lien Paydown from Rights Offering	100,000	100,000
Total Consideration to Beal Bank	**$508,019**	**$508,019**
First Lien Debt Claim at Confirmation [(5)]	**$484,110**	**$484,110**
Recharacterization [(6)]	-	(29,651)
First Lien Debt Claim	**$484,110**	**$454,459**
First Lien Debt Recovery %	**104.9%**	**111.8%**

(1) Represents the Ad Hoc Committee's midpoint of the TEV range, which has been adopted by Beal Bank.

(2) Per the Debtors' prior Disclosure Statement.

(3) Includes $125 million of cash from the rights offering paid to the Debtors per the Beal Plan less $13.9 million.

(4) Represents the new common stock to be received by Beal Bank and its designees under the Beal Plan assuming the rights offering is wholly unsubscribed less the percentage of common stock that Beal Bank agreed to purchase pursuant to its backstop agreement, and further assumes that the Second Lien Noteholders and general unsecured creditors will receive, in lieu of 2.01% of the new equity, $13.9 million in cash. The figure is extrapolated from the information contained on page 18 of the Beal Disclosure Statement (although the share percentages depicted in that table total more than 100%).

(5) Calculated based upon the current balance of the pre-petition Beal Bank debt outstanding as reflected in the October Monthly Operating Report filed with the Bankruptcy Court less the scheduled $1.2 million amortization payment due to be made at year's-end.

(6) Includes interest payments made to Beal Bank since February 17, 2009 (including the scheduled year-end payment) plus $4 million of estimated professional fees paid to Beal Bank, less the amount by which Beal Bank is over-secured.

31. Beal Bank appears to have reverse-engineered its plan by, first, arbitrarily capping the recovery to Second Lien Noteholders simply based on the value ascribed by Beal Bank to the Second Lien Noteholders' recovery under the AHC Plan (without applying a discount to take into the fact that the stock issued under the Beal Plan represents a minority and illiquid stake). Beal Bank then offers to fully equitize its debt, even though it is over-secured, in the thinly-veiled attempt to persuade creditors and the Court that its plan offers the prospect of a deleveraged balance sheet and is "more" feasible than the AHC Plan—a legally insignificant factor given the absence of creditor support for the Beal Plan and the obvious feasibility of the AHC Plan.

32. Another fiction lies with Beal Bank's determination to allocate a portion of its own equity as a backstop fee. Realistically, the Beal Plan is nothing more than a credit bid coupled with a $125 million cash equity investment. Beal Bank's rights offering represents a hollow offer to creditors to buy illiquid stock in a company controlled by a regulated bank. As such, Beal Bank cannot reasonably expect that holders would chose to invest in a privately-held company controlled by it (and the Ad Hoc Committee is certainly committed to vote against the Beal Plan). The result is, in substance, an effective foreclosure upon the Debtors' assets. Whether Beal Bank characterizes a portion of its own stock as a backstop fee is irrelevant or without substance.

C. Beal Bank Fails to Apprise Creditors and this Court of Key Risk Factors, Such as the Ability of Beal Bank to Influence and Control the Reorganized Debtors and to Cause the Reorganized Debtor to Incur Indebtedness

33. Beal Bank's main pitch to this Court and creditors is that its plan offers a complete deleveraging of the balance sheet and improves the cash flow of the reorganized Debtors. However, Beal Bank plays down the fact that, under the Beal Plan: (a) the reorganized Debtors will be a private non-reporting company; (b) Beal Bank (and its affiliates) would hold,

at a minimum, more than two-thirds of the new common stock of NewCo (assuming the Beal rights offering is *fully* subscribed);[7] (c) a wholly-owned subsidiary of Beal Bank will be entitled to receive the sole share of preferred stock issued by NewCo, thereby conferring upon Beal Bank a veto right with respect to "certain actions to be taken by NewCo"; and (d) Beal Bank will be entitled to control the new Board of Directors. Thus, under all circumstances, Beal Bank will be in control of the reorganized Debtors, and will have nearly unfettered power to direct the operations of the company. Beal Bank will be able to cause the reorganized Debtors to incur indebtedness, issue dividends or make other restricted payments, or engage in affiliate or other transactions that would prejudice minority shareholders or employees, such as dilutive issuances of new stock. The notion that the Beal Plan represents a superior proposal that offers greater long term benefit to stakeholders is simply misleading. Beal Bank must be required to provide additional disclosure relating to potential risks to minority shareholders associated with equity ownership under the Beal Plan and the fact that creditors will have no voice as minority shareholders in a private company.

D. Additional Failure to Make Adequate Disclosure

34. The Beal Disclosure Statement also lacks adequate disclosure in respect of the following:

- ***Mischaracterization of the terms of the AHC Plan:*** The Beal Disclosure Statement fails to appropriately describe the terms of the AHC Plan. As of the filing of this Objection, the Ad Hoc Committee is in the process of amending the AHC Plan to account for the addition of the Debtors as co-plan proponents, and will provide appropriate language to counsel to Beal Bank to address this concern.

[7] The precise equity capitalization under the Beal Plan on a pro forma basis is unclear from the Beal Disclosure Statement. In fact, the capitalization chart found on page 18 of the Beal Disclosure Statement totals more than 100% of the new common stock. Beal Bank must be required to clarify the percentages of potential equity ownership under the Beal Plan.

- ***Estimated Effective Date:*** Beal Bank states that the effective date under the Beal Plan is anticipated by Beal Bank to occur in January 2010 subject to further litigation regarding the plan and gaming regulatory approvals. Beal Bank's estimate is entirely unrealistic and fails to take into account that the Interim Casino Authorization provisions of the New Jersey Casino Control Act contemplate a 120-day period during which the New Jersey Control Commission could conduct its investigation (though approvals could come sooner). The estimate also fails to take into account the notice and approval requirements under applicable banking regulations.

- ***2% Equity Distribution Under the Beal Plan is Illusory:*** The Beal Plan proposes a distribution of approximately 2% of the reorganized equity to Second Lien Noteholders and general unsecured creditors unless less than 50% of the Beal Bank rights offering stock is subscribed to by Second Lien Noteholders and general unsecured creditors, in which case, in lieu of equity, the Second Lien Noteholders and general unsecured creditors would be entitled to receive $13.9 million in cash instead. However, as Beal Bank is aware, the Ad Hoc Committee holds more than 61% of the principal amount outstanding under the Second Lien Notes and is committed to the AHC Plan, and thus will not be participating in the Beal Bank rights offering. Thus, the 2% equity distribution is illusory. The Bank Disclosure Statement should therefore be modified to reflect the unlikely outcome that Second Lien Noteholders and general unsecured creditors would receive the 2% equity distribution under the Bank Plan.

- ***Treatment of Trump Brand Under the Beal Plan:*** As this Court is aware, Beal Bank had previously sponsored a plan of reorganization that was conditioned upon the financial contribution of Donald Trump as well as the continued use of the Trump brand and the value enhancement to be gained from Mr. Trump's continued participation in the Debtors' businesses. *See Beal Bank Appellate Opening Brief* at p.7 ("Based on Beal Bank's belief that the ongoing and active participation in the business of the Debtors' former celebrity owner, Donald Trump (and his daughter, Ivanka), would maximize its recovery, the Beal Bank proposal was conditioned upon the Trumps' commitment to participate in the restructuring. In contrast, the Ad Hoc Committee's proposal would have left the Debtors' casinos to compete in an increasingly chaotic and competitive Atlantic City gaming market bereft of their most distinguishing feature, namely the Trump brand."); *see also Stay Motion* at ¶ 5. Donald and Ivanka Trump have now withdrawn from that plan, and Beal Bank has proposed a new plan that lacks the consensual use of the Trump brand. Beal Bank should be required to explain its position with respect to the Trademark License Agreement and the impact of the withdrawal of support from Donald Trump. Although Beal Bank now adopts the Ad Hoc Committee's valuation, Beal Bank should be required to explain how Donald Trump's withdrawal from the plan previously supported by Beal Bank impacts Beal Bank's view of the future value of the Debtors' businesses so that creditors can have an apples-to-apples comparison of the respective plans.

- ***Gaming Investments:*** Beal Bank has deleted disclosure previously made in the Debtors' prior disclosure statement regarding investments in gaming and casino operations, which must be restored.

- ***Basis for Two-Step Closing Process:*** The Beal Plan provides for a two-step closing process, by which all claims *other than the First Lien Lender Claims* stand to be discharged upon the first closing date (*i.e.*, the Effective Date), with the second closing date to occur on the following business day. No explanation is given for the preferential treatment afforded to Beal Bank or the reasons for the two-step process.

CONCLUSION

35. The Ad Hoc Committee appreciates the opportunity given to all parties in interest to file competing plans now that exclusivity has been lifted. That opportunity, however, cannot be misused to permit Beal Bank to proceed with a plan that it knows it cannot consummate. In reality, Beal Bank has no genuine interest in acquiring the equity of the Debtors, and, the Ad Hoc Committee submits, the Beal Plan has not been filed in good faith, but instead represents nothing more than a futile attempt by the bank, without support from the Debtors or any other major constituency in the case, to extract unrealistic and unprecedented concessions from the Ad Hoc Committee to improve Beal Bank's treatment under the AHC Plan. Based on the foregoing, the Ad Hoc Committee respectfully requests that Court reject the Beal Disclosure Statement.

WHEREFORE, based on the foregoing, the Ad Hoc Committee respectfully requests that the Court reject the Beal Disclosure Statement and grant the Ad Hoc Committee such other relief as the Court deems proper.

Dated: December 9, 2009

Respectfully submitted,

LOWENSTEIN SANDLER PC

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Co-Counsel to the Ad Hoc Committee of Holders of 8.5% Senior Secured Notes Due 2015

ANNEX A

1988 WL 1021862 (O.T.S.)

Office of Thrift Supervision (OTS)

DATE: January 27, 1988

ADDRESSEE: Joseph M. Arendes, Deputy Director, Office of Regulatory, Policy, Oversight, and Supervision
AUTHOR: Julie L. Williams, Deputy General Counsel, for Securities and Corporate Structure

SUBJECT: Service Corporation Investments Pursuant to Salvage Powers

This responds to your memorandum of December 1, 1987, transmitting a request dated November 12, 1987, from Supervisory Agent John Gilbert of the Federal Home Loan Bank of Atlanta for an opinion with respect to a number of issues regarding how to properly calculate the present aggregate outstanding investment in service corporations of Federal Savings and Loan Association, * * * (the "Association"), and the effect, if any, upon the Association's aggregate outstanding service corporation investment of a proposed investment by the Association in bonds to be issued by a municipal taxing district to finance improvements to building lots in a development project in which service corporations of the Association hold substantial interests.

Background
In the 1970s and early 1980s, the Association made six loans totaling $23.4 million to * * * Inc., an unaffiliated land development and marketing firm. The loans, which were for the purpose of developing two large residential development projects located in central Florida, were secured by contract for deed receivables and the project property. By the end of 1984, * * * was experiencing serious financial difficulties.

In an effort to alleviate * * *'s financial difficulties, the Association, in the Spring of 1985, caused one of its wholly-owned service corporations known as * * * Company to purchase from * * * for approximately $8.8 million substantially all of the lots in the projects zoned for commercial and mobile home development. Shortly thereafter, however, * * * again faced severe financial pressures, at which point the sole shareholders of * * * and his wife, offered to sell all of the outstanding stock of * * * to the Association in exchange for $1 and the release of * * * and his wife from their personal guarantees. The Association decided to accept the * * *'s offer, rather than to await default and foreclose on the loans, because the Association believed that foreclosure would result in revocation of the permits and licenses necessary to complete the projects and would force * * * into bankruptcy, thereby forcing significant delays in completing the projects and making marketing substantially more difficult.

In an examination of the Association in the Spring of 1986, the Association's Supervisory Agent ("SA") concluded that the acquisition of * * * did not represent a proper exercise of the Association's salvage powers and, therefore, that such acquisition must be viewed as a routine service corporation acquisition subject to 12 C.F.R. Section 545.74. As a result, the SA concluded that the Association's total investments in service corporations for purposes of 12 C.F.R. Section 545.74 * * * million or 4.3% of assets) was in excess of permissible levels. The basis for the SA's conclusion that the acquisition of * * * was not a proper exercise of the Association's salvage powers is set forth on page 3 of the SA's November 12, 1987, memorandum to ORPOS:

> [W]e understand [that past OGC opinions have indicated] that a federal association may transfer to a service corporation REO acquired through foreclosure or deed in lieu and undertake investments in that service corporation for the sole purpose of salvaging that asset, notwithstanding the investment limitations imposed by

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> Section 545.74(d) and without approval under Section 563.38.... [F]or various reasons, [however,] * * * chose to acquire the stock of rather than to foreclose on the property securing its loans to * * * and pursuing * * *'s owners under their personal guarantees. We believe that * * * acquisition of the * * * stock in consideration for the release of the guarantors represents a materially different factual situation than those addressed in the above-referenced opinion[s].... * * *'s acquisition of the stock of the borrower as opposed to taking title to the security property appears to us to represent a separate investment decision from the initial granting of the loans. Additionally, in acquiring the service corporation, the institution acquired substantial liabilities, including the development obligations of * * * and its contingent liability for refund of contract payments, which it would not have acquired if it had taken title to the property through foreclosure or deed in lieu. While the Association may have no direct exposure relative to these liabilities, apart from its loans and investments in the service corporation, the potential for litigation in this area and the magnitude of the liabilities involved, in our view, increases the Association's risk of loss above the amount of its initial loans on the projects.

Instead of challenging the SA's salvage powers conclusion, the Association argued that the loans to should not be counted as service corporation investments within the meaning of 12 C.F.R. Section 545.74(d)(1) because they qualified for the exception carved out at 12 C.F.R. Section 545.74(d)(2)(ii), i.e., immediately following the acquisition of * * * by the Association (i) the Association's regulatory capital was in compliance with 12 C.F.R. Section 563.13; (ii) the Association's scheduled items were less than 2.5% of specified assets; (iii) the loans to * * * consisted of conforming loans within the meaning of 12 C.F.R. Section 545.74(a)(2); and (iv) these conforming loans did not exceed 50% of the Association's regulatory capital. The SA took the position that these loans did not constitute conforming loans since "in acquiring the stock [of * * *, the Association] acquired liabilities of [* * *] which were not attached to the security property, [and, therefore, the Association] has assumed a position materially different from that of a normal lender." SA's November 12, 1987, memorandum to ORPOS, at p. 6. Accordingly, the SA concluded that all of the loans to * * * had to be counted as service corporation investments subject to the limitations of Section 545.74(d)(1), and the Association was instructed to begin decreasing its service corporation investments.

Since that time, the Association has reduced, by approximately $4.5 million, the amount of service corporation investments carried on its books by means of writedowns reflecting the amount of its equity participation in the net losses of its service corporations and the establishment of specific loss reserves with respect to service corporation investments. The Association maintains that these writedowns and loss reserves reduce the amount of the Association's investments under Section 545.74(d)(1). The SA disagrees. The Association also continues to insist that the loans to * * * qualify for the exception set forth in Section 545.74(d)(2)(ii). As of July 31, 1987, the amount of Association's service corporation investments in excess of the limitations set forth in Section 545.74(d)(1), as computed by the SA, was approximately $22.5 million. Under the Association's assumptions, the amount of excess investments was only approximately $4.2 million.

The Association has advised the SA that virtually all of the properties that have been sold in the projects owned by CFD were sold pursuant to installment contracts that provide for refunds of contract payments and accrued interest in the event the local taxing district fails to make certain improvements (i.e., roads and drainage) to the properties within a specified time. With respect to most of the properties that have been sold, the applicable time periods have expired without the necessary improvements being made. The Association has advised the SA that unless the improvements are completed quickly, * * * is likely to receive numerous refund requests. If all of the purchasers entitled to do so requested refunds, the amount due could reach $65 million. In addition, the Florida Division of Land Sales has advised * * * that it may revoke * * *'s permits and bar * * * from delivering title to any of the as yet unsold lots in the projects unless * * * comes up with a workable plan for completing development of the projects in the near future.

Since * * * still holds title to over half of the properties within the taxing district that encompasses the projects, * * * has effective voting control of the board that governs the taxing district and, therefore, is in a position to cause the district to issue development bonds to finance the necessary improvements. The source of payment for any such bonds, however, would be funds raised by the taxing district from taxes levied on the property owners in the projects

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and, in some cases, the project developer. Since * * * is both the project developer and largest property owner in the projects and * * * is currently insolvent, there is no current market for the taxing district's bonds. In the absence of such a market, the Association has proposed to purchase $3 million of the bonds itself.

The SA has advised the Association that, in his view, such a purchase might constitute a further investment in service corporations, and that, since the Association's service corporation investments already exceed permissible limits, any further service corporation investment would be permissible only if the investment is approved in advance pursuant to 12 C.F.R. Section 563.38(a) (salvage powers application). The Association maintains that the purchase of the bonds would not constitute a service corporation investment, but rather an investment in the obligations of a political subdivision of a state government, as permitted by 12 C.F.R. Section 545.72(b). In the alternative, the Association maintains that its method of computing service corporation investments is correct and, therefore, if and when it takes additional loss reserves or writedowns on its service corporation investments, those reserves and writedowns should be deemed to reduce the Association's service corporation investments, thereby providing the Association with additional service corporation investment authority to the extent such reserves and writedowns reduce the Association's service corporation investments below the limitations specified in Section 545.74(d)(1).

Discussion

Although the foregoing facts raise a variety of issues regarding the proper method of computing service corporation investments under Section 545.74, the first and most fundamental question presented by this case is whether the Association's acquisition of * * * constituted a proper exercise of the Association's salvage powers. If it did, then neither the Association's investments in * * * at the time of acquisition nor any subsequent investments necessary to complete the salvage operation would be counted as part of the Association's aggregate outstanding investment in service corporations for purposes of Section 545.74(d). O.G.C. Mem. to Board, May 1, 1975 (including attached Int.G.C.Mem., March 12, 1975) (investments in service corporations that are made as part of a bona fide salvage operation are not investments made “under” 12 U.S.C. Section 1464(c)(4)(B) and 12 C.F.R. Section 545.74; such investments are made pursuant to the implied powers of federal associations); for other opinions to the same effect, see Op.G.C., July 22, 1987, at pp. 4–5; and Op.G.C., November 25, 1986, at p. 2. Since the Association's investments in * * * at the time of acquisition constitute the bulk of the Association's service corporation investments, a conclusion that the * * * acquisition was a proper exercise of the Association's salvage powers and, therefore, not subject to Section 545.74, would effectively moot all of the technical Section 545.74 computational issues described above.

Past opinions of this Office regarding the salvage powers of federal associations have held that federal associations have implied power to make investments not authorized under their express powers in order to salvage existing investments, provided such investments (i) do not contravene a specific legal prohibition or fundamental public policy; and (ii) are an integral part of a reasonable and bona fide salvage operation. E.g., Op.G.C., July 22, 1987, at pp. 4–5. As noted above, the SA concluded, in this case, that the Association's acquisition of * * * could not be characterized as bona fide salvage operation. Although the SA acknowledges that a federal association may, pursuant to its salvage powers and irrespective of the limitations of Sections 545.74 and 563.38, acquire real estate in foreclosure-type situations and then transfer that real estate to a service corporation for management and disposition, the SA concluded that a federal association may not, pursuant to its salvage powers, elect instead to acquire the stock of the borrower outright. Such an acquisition, the SA reasoned, represents a separate investment decision resulting in an increase in the potential exposure of the federal association, rather than a mere attempt to wind down (i.e., salvage) an existing investment, and, accordingly, cannot be characterized as part of a bona fide salvage operation. SA's November 12, 1987, memorandum to ORPOS, at p. 3. As a general rule, this Office defers to the SA to determine whether a particular investment is part of a bona fide salvage operation, since such determinations usually turn on the unique facts of each case. In the present case, however, it appears that the SA's determination was based upon a legal premise (i.e., acquisition of the stock of a borrower in lieu of foreclosure is ipso facto not a proper exercise of salvage powers) that is at odds with the existing salvage powers case law.

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Although there are not many cases that have considered what constitutes a proper exercise of the salvage powers of financial institutions, the facts of several of the cases that have been decided bear a close resemblance to those recited above in this memorandum. In Atherton v. Anderson, 86 F.2d 518 (6th Cir.1936), the Sixth Circuit Court of Appeals considered whether a national bank had acted unlawfully when it acquired all of the assets of one of its borrowers, the Kentucky Wagon Manufacturing Company, with a view toward operating the company as a going concern until it could be resold, instead of awaiting the results of bankruptcy proceedings, which were expected to net the bank 25 cents on the dollar. Notwithstanding the fact that the bank had to make an additional $300,000 investment to acquire the assets of the borrower (thereby incurring substantial additional risk of loss), the court held as follows:

> It is true that a national bank has no authority to engage in or promote a purely speculative business. It has generally been thought, however, and we think the view is nowhere seriously disputed, that a bank has implied power when faced with a loss growing out of a legitimate banking transaction to acquire stocks or other property when it is honestly believed at the time that under more favorable circumstances a loss which would otherwise accrue might be averted or diminished. [A]s an incident to its express powers the bank has a right to acquire property, to put it in condition for resale, and where such property is a manufacturing establishment whose value depends substantially upon uninterrupted operation, we think implied power exists to continue such operation providing the primary purpose of the bank is to save its debt rather than to speculate in future profits and there is a reasonable prospect of realization of profits.... [M]uch must be left to the business judgment of those responsible for ... solution [of the problem] if such judgment is honestly exercised. Id. at 525 (emphasis added).

In Eureka Building and Loan Association v. Greenwood Hotel Corporation, 103 P.2d 46 (Kan.1940), the Kansas Supreme Court considered whether a state building and loan association acted unlawfully when, instead of foreclosing upon a mortgage loan on a hotel, it instead participated in the formation of a corporation to hold and operate the hotel. One-third of the stock of the corporation was distributed to the association, with the other two-thirds going to the two individuals who were previously sole owners of the hotel. A new mortgage on the hotel was issued to the association by the corporation. Later, when the association attempted to foreclose on that new mortgage, the two individuals argued that the mortgage was unenforceable on grounds that the whole scheme (i.e., the association's investment in the corporation) was illegal since the association lacked legal authority to invest in hotel corporations. In responding, the court commented as follows:

> An instructive case on this subject, well fortified by authority, was Fidelity Ins. Co. v. German Sav. Bank ... where an insurance company took stock in an insolvent bank in an effort to save itself from a loss. Later an assessment was made on the bank stock which the insurance company sought to evade on a plea of ultra vires. Section 4 of the syllabus [of the court's decision] reads: “Although a transaction of a corporation may not be strictly within its grant of power, yet if made to save the corporation from loss the plea of ultra vires will not avail, where the agreement has been carried out and is not expressly prohibited or contrary to public policy....” The plea of ultra vires cannot be successfully invoked against a plaintiff creditor for taking whatever reasonable and practical steps its sees fit to save itself from loss, unless some express provision of statute forbids. Id. 50–51.

On the basis of the foregoing cases, we conclude that the acquisition of the stock of a borrower, in lieu of foreclosure, should be deemed to be part of a bona fide salvage operation if and when circumstances at the time of the acquisition are such that a reasonable business person could conclude that acquisition of the borrower's stock is the best way for the association to minimize or avoid loss on its loan. Whether this standard is met in each particular case is, of course, a matter for the determination of the SA. It should be stressed, however, that the question to be decided by the SA is not whether the SA believes that acquisition of the stock of the borrower is the best solution to the problem, but whether the SA believes that a reasonable business person could so conclude. Atherton v. Anderson, 86 F.2d at 525. The fact that the acquisition of stock may result in an even greater loss to the association if the salvage scheme fails is not, of itself, a presumptive disqualifier, provided there is a reasonable prospect that the association's prospective loss on its investment will be reduced if the salvage scheme succeeds. Atherton v. Anderson, supra; Eureka v. Greenwood, 103 P.2d 46. As was noted in a previous opinion of this Office, “It is, of course, inherent in any salvage operation that the result may simply be greater loss, but this fact does not require or justify prohi-

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bition of salvage operations." Int.G.C.Mem., March 12, 1975, at p. 8 (attached to O.G.C.Mem. to Board, May 1, 1975).

We recommend that a copy of this opinion be forwarded to the SA and that the SA be asked to re-review the facts surrounding the Association's acquisition of * * * in light of the legal standards established in the court cases described above. Based on the limited information available to us, it appears that those standards were probably met at the time of the acquisition. If the SA is aware of additional facts suggesting that the standards may not have been met, we recommend that he contact this Office to discuss those additional facts.

Provided the standards of the case law are met, it follows that the Association's acquisition of * * * was part of a bona fide salvage operation and that, therefore, the Association was free to make that acquisition and may make additional investments in * * * that are reasonably calculated to complete the salvage operation, provided such acquisition did not and such additional investments do not contravene any specific legal prohibition or fundamental public policy. As already noted above, past opinions of this Office have concluded that Section 545.74 does not constitute a specific legal prohibition in the context of salvage operations. That leaves only two other specific regulatory provisions to be considered: 12 C.F.R. Sections 563.9–8 and 563.38(a). The restrictions of Section 563.9–8 do not come into play in this case because the Association's level of equity risk investments is and has been far below the maximum permissible level of such investments. (The Association's current total equity risk investments are * * * million; the Association's current maximum permissible amount of equity risk investments is * * * million.) The restrictions of Section 563.38 also do not apply in this case. Previous opinions of this Office have held that Section 563.38(a) applies only to additional investments in existing service corporations that were initially acquired for reasons unrelated to salvaging other non-service corporation investments. E.g., Op.G.C., July 22, 1987, at p. 5. Section 563.38(a) does not apply to initial and additional investments in service corporations formed or acquired in order to facilitate the salvage of non-service corporation investments (e.g., real estate loans). Id. Thus, it appears that the only question that the SA must consider upon review is whether the Association's acquisition of constituted a a bona fide salvage operation within the meaning of the cases described above. If so, then the acquisition was a proper and lawful exercise of the Association's salvage powers.[FN1]

If there are any questions regarding the foregoing, please feel free to contact Jeff Miner, Staff Attorney, at (202) 377–7546.

FN1 Although the appropriate classification of the Association's investment in * * * has apparently not been a part of the dispute between the SA and the Association, we note in passing that the determination whether that investment constituted part of a bona fide salvage operation should also be governed by the standards established in the cases described above.

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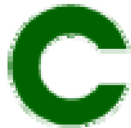
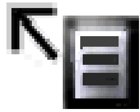
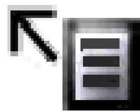


Effective:[See Text Amendments]

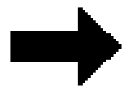
Code of Federal Regulations Currentness
Title 12. Banks and Banking
Chapter V. Office of Thrift Supervision, Department of the Treasury (Refs & Annos)



Part 559. Subordinate Organizations (Refs & Annos)



Subpart B. Regulations Applicable to All Savings Associations



§ 559.13 How may a savings association exercise its salvage power in connection with a service corporation or lower-tier entities?

(a) In accordance with this section, a savings association ("you") may exercise your salvage power to make a contribution or a loan (including a guarantee of a loan made by any other person) to your service corporation or lower-tier entity ("salvage investment") that exceeds the maximum amount otherwise permitted under law or regulation. You must notify OTS at least 30 days before making such a salvage investment. This notice must demonstrate that:

(1) The salvage investment protects your interest in the service corporation or lower-tier entity;

(2) The salvage investment is consistent with safety and soundness; and

(3) You considered alternatives to the salvage investment and determined that such alternatives would not adequately satisfy paragraphs (a)(1) and (a)(2) of this section.

(b) If OTS notifies you within 30 days that the Notice presents supervisory concerns, or raises significant issues of law or policy, you must apply for and receive OTS's prior written approval under the standard treatment processing procedures at part 516, subparts A and E of this chapter before making a salvage investment.

(c) If your service corporation or lower-tier entity is a GAAP-consolidated subsidiary, your salvage investment under this section will be considered an investment in a subsidiary for purposes of part 567 of this chapter.

[66 FR 13007, March 2, 2001]

SOURCE: 59 FR 18475, April 19, 1994; 60 FR 66715, Dec. 26, 1995; 61 FR 575, Jan. 8, 1996; 61 FR 66571, Dec. 18, 1996, unless otherwise noted.

AUTHORITY: 12 U.S.C. 1462, 1462a, 1463, 1464, 1828.

12 C. F. R. § 559.13, 12 CFR § 559.13

Current through November 25, 2009; 74 FR 62188

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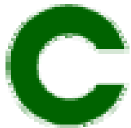
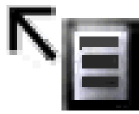
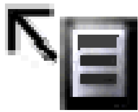


Effective:[See Text Amendments]

Code of Federal Regulations Currentness
Title 12. Banks and Banking
Chapter III. Federal Deposit Insurance Corporation (Refs & Annos)
Subchapter B. Regulations and Statements of General Policy



Part 362. Activities of Insured State Banks and Insured Savings Associations (Refs & Annos)



Subpart D. Acquiring, Establishing, or Conducting New Activities through a Subsidiary by an Insured Savings Association

§ 362.15 Acquiring or establishing a subsidiary; conducting new activities through a subsidiary.

No state or Federal insured savings association may establish or acquire a subsidiary, or conduct any new activity through a subsidiary, unless it files a notice in compliance with § 303.142(c) of this chapter at least 30 days prior to establishment of the subsidiary or commencement of the activity and the FDIC does not object to the notice. This requirement does not apply to any Federal savings bank that was chartered prior to October 15, 1982, as a savings bank under State law or any savings association that acquired its principal assets from such an institution.

SOURCE: 63 FR 66326, Dec. 1, 1998; 65 FR 15530, March 23, 2000; 66 FR 1028, Jan. 5, 2001, unless otherwise noted.

AUTHORITY: 12 U.S.C. 1816, 1818, 1819(a) (Tenth), 1828(j), 1828(m), 1828a, 1831a, 1831e, 1831w, 1843(l).

12 C. F. R. § 362.15, 12 CFR § 362.15

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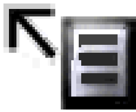
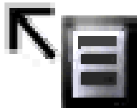
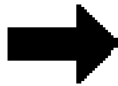
West's Nevada Revised Statutes Annotated Currentness
Title 55. Banks and Related Organizations

 Chapter 662. Powers and Miscellaneous Provisions (Refs & Annos)

 Investments; Reserves; Loan Limits



662.135. Limitations on investment in stock of or membership in other banks and business organizations

1. Except as otherwise provided in this section and subject to the provisions of NRS 662.065 and 662.125, no bank may make any investment in the stock or become a member of any other state or national bank.

2. A bank doing business under this title may subscribe to or purchase, upon such terms as may be agreed upon, the stock of banks organized under the Act of Congress known as the Edge Act or the stock of central reserve banks whose stock exceeds $1,000,000.

3. To constitute a central reserve bank as contemplated by this title, at least 50 percent of the capital stock of the bank must be owned by other banks. The investment by any bank in the capital stock of a central reserve bank or a bank organized under the Edge Act, must at no time exceed 10 percent of the stockholders' or members' equity of the bank making the investment.

4. A bank shall not invest in the stocks or ownership of other corporations, firms, partnerships or companies except as otherwise provided in this title, unless the investment is made to protect the bank from loss.

5. A bank may invest in the stocks or ownership of other corporations, firms, partnerships or companies as part of a merger, consolidation, combination or acquisition that is authorized pursuant to the provisions of chapter 78, 86 or 92A of NRS, regardless of whether the investment is made to protect the bank from loss.

6. Any stocks or ownership owned or acquired after July 1, 1971, in excess of the limitations imposed by this section must be disposed of at public or private sale within 12 months after the date of acquiring them, and if not so disposed of, they must be charged to profit and loss account, and no longer carried on the books as an asset. The limit of time in which such stocks or ownership is disposed of or charged off the books of the bank may be extended by the Commissioner if in his judgment it is for the best interest of the bank that an extension be granted.

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7. A bank may subscribe to, purchase or become the owner of stock in:

(a) Federal reserve banks as established by Act of Congress approved December 23, 1913, being c. 6, 38 Stat. 251, or any amendment thereof; or

(b) Any governmental agency, Federal Home Loan Bank or liquidating or financial corporation created by the Congress of the United States.

8. A bank may invest up to 50 percent of its surplus in the stock or membership of corporations or limited-liability companies engaged in related banking fields.

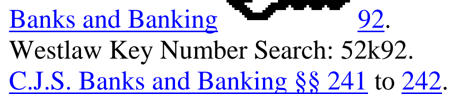
CREDIT(S)

Added by Laws 1971, p. 984. Amended by Laws 1983, p. 1739; Laws 1987, p. 1916; Laws 1995, p. 486; Laws 1997, p. 990.

HISTORICAL AND STATUTORY NOTES

Laws 1997, c. 286 took effect July 3, 1997.

LIBRARY REFERENCES

Banks and Banking  92.
Westlaw Key Number Search: 52k92.
C.J.S. Banks and Banking §§ 241 to 242.

N. R. S. 662.135, NV ST 662.135

Current through the 2007 74th Regular Session and the 25th Special Session (2008) of the Nevada Legislature and technical corrections received from the Legislative Counsel Bureau through the 25th Special Session (2008).

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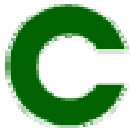
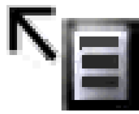
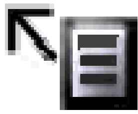


Effective: April 21, 2006

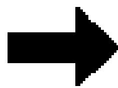
Code of Federal Regulations Currentness
Title 12. Banks and Banking
Chapter III. Federal Deposit Insurance Corporation (Refs & Annos)
Subchapter B. Regulations and Statements of General Policy



Part 362. Activities of Insured State Banks and Insured Savings Associations (Refs & Annos)



Subpart A. Activities of Insured State Banks



§ 362.4 Subsidiaries of insured State banks.

(a) Prohibition. A subsidiary of an insured State bank may not engage as principal in any activity that is not of a type permissible for a subsidiary of a national bank, unless it meets one of the exceptions in paragraph (b) of this section.

(b) Exceptions--

(1) Consent obtained through application. A subsidiary of an insured State bank may conduct otherwise prohibited activities if the bank obtains the FDIC's prior written consent and the insured State bank meets and continues to meet the applicable capital standards set by the appropriate Federal banking agency. Consent will be given only if the FDIC determines that the activity poses no significant risk to the Deposit Insurance Fund. Applications for consent should be filed in accordance with § 303.121 of this chapter and will be processed under § 303.122(b) of this chapter. Approvals granted under § 303.122(b) of this chapter may be made subject to any conditions or restrictions found by the FDIC to be necessary to protect the Deposit Insurance Fund from risk, to prevent unsafe or unsound banking practices, and/or to ensure that the activity is consistent with the purposes of Federal deposit insurance and other applicable law.

(2) Grandfathered insurance underwriting subsidiaries. A subsidiary of an insured State bank may:

(i) Engage in grandfathered insurance underwriting if the insured State bank or its subsidiary on November 21, 1991, was lawfully providing insurance as principal. The subsidiary may continue to provide the same types of insurance as principal to the residents of the State or states in which the bank or subsidiary did so on such date provided that:

(A)(1) The bank meets the capital requirements of paragraph (e) of this section; and

(2) The subsidiary is an “eligible subsidiary” as described in paragraph (c)(2) of this section; or

(B) The bank submits an application in compliance with § 303.121 of this chapter and the FDIC grants its consent under the procedures in § 303.122(b) of this chapter.

(ii) Continue to provide as principal title insur-

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ance, provided the bank was required before June 1, 1991, to provide title insurance as a condition of the bank's initial chartering under State law and neither the bank nor its parent holding company undergoes a change in control.

(iii) May continue to provide as principal insurance which is reinsured in whole or in part by the Federal Crop Insurance Corporation if the subsidiary was engaged in the activity on or before September 30, 1991.

(3) Majority-owned subsidiaries' ownership of equity investments that represent a control interest in a company. The FDIC has determined that investment in the following by a majority-owned subsidiary of an insured State bank does not represent a significant risk to the Deposit Insurance Fund:

(i) Equity investment in a company engaged in real estate or securities activities authorized in paragraph (b)(5) of this section if the bank complies with the following restrictions and files a notice in compliance with § 303.121 of this chapter and the FDIC processes the notice without objection under § 303.122(a) of this chapter. The FDIC is not precluded from taking any appropriate action or imposing additional requirements with respect to the activity if the facts and circumstances warrant such action. If changes to the management or business plan of the company at any time result in material changes to the nature of the company's business or the manner in which its business is conducted, the insured State bank shall advise the appropriate regional director (DSC) in writing within 10 business days after such change. Investment under this paragraph is authorized if:

(A) The majority-owned subsidiary controls the company;

(B) The bank meets the core eligibility criteria of paragraph (c)(1) of this section;

(C) The majority-owned subsidiary meets the core eligibility criteria of paragraph (c)(2) of this section (including any modifications thereof applicable under paragraph (b)(5)(i) of this section), or the company is a corporation meeting such criteria;

(D) The bank's transactions with the majority-owned subsidiary, and the bank's transactions with the company, comply with the investment and transaction limits of paragraph (d) of this section;

(E) The bank complies with the capital requirements of paragraph (e) of this section with respect to the majority-owned subsidiary and the company; and

(F) To the extent the company is engaged in securities activities authorized by paragraph (b)(5)(ii) of this section, the bank and the company comply with the additional requirements therein as if the company were a majority-owned subsidiary.

(ii) Equity securities of a company engaged in the following activities, if the majority-owned subsidiary controls the company or the company is controlled by insured depository institutions, and the bank meets and continues to meet the applicable capital standards as prescribed by the appropriate Federal banking agency. The FDIC consents that a majority-owned subsidiary may conduct such activity without first obtaining the FDIC's consent. The fact that prior consent is not required by this subpart does not preclude the FDIC from taking any appropriate action with respect to the activity if the facts and circumstances warrant such action:

(A) Any activity that is permissible for a national bank, including such permissible activities that may require the company to register as a securities broker;

(B) Acting as an insurance agency;

(C) Engaging in any activity permissible for an insured State bank under § 362.3(b)(2)(iii) to the same extent permissible for the insured bank thereunder, so long as instruments held under this paragraph (b)(3)(ii)(C), paragraph (b)(7) of this section, and § 362.3(b)(2)(iii) in the aggregate do not exceed the limit set by §

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362.3(b)(2)(iii);

(D) Engaging in any activity permissible for a majority-owned subsidiary of an insured State bank under paragraph (b)(6) of this section to the same extent and manner permissible for the majority-owned subsidiary thereunder; and

(4) Majority-owned subsidiary's ownership of certain securities that do not represent a control interest--

(i) Grandfathered investments in common or preferred stock and shares of investment companies. Any insured State bank that has received approval to invest in common or preferred stock or shares of an investment company pursuant to § 362.3(a)(2)(iii) may conduct the approved investment activities through a majority-owned subsidiary of the bank without any additional approval from the FDIC provided that any conditions or restrictions imposed with regard to the approval granted under § 362.3(a)(2)(iii) are met.

(ii) Bank stock. An insured State bank may indirectly through a majority-owned subsidiary organized for such purpose invest in up to ten percent of the outstanding stock of another insured bank.

(5) Majority-owned subsidiaries conducting real estate investment activities and securities underwriting. The FDIC has determined that the following activities do not represent a significant risk to the Deposit Insurance Fund, provided that the activities are conducted by a majority-owned subsidiary of an insured State bank in compliance with the core eligibility requirements listed in paragraph (c) of this section; any additional requirements listed in paragraph (b)(5)(i) or (ii) of this section; the bank complies with the investment and transaction limitations of paragraph (d) of this section; and the bank meets the capital requirements of paragraph (e) of this section. The FDIC consents that these listed activities may be conducted by a majority-owned subsidiary of an insured State bank if the bank files a notice in compliance with § 303.121 of this chapter and the FDIC processes the notice without objection under § 303.122(a) of this chapter. The FDIC is not precluded from taking any appropriate action or imposing additional requirements with respect to the activities if the facts and circumstances warrant such action. If changes to the management or business plan of the majority-owned subsidiary at any time result in material changes to the nature of the majority-owned subsidiary's business or the manner in which its business is conducted, the insured State bank shall advise the appropriate regional director (DSC) in writing within 10 business days after such change. Such a majority-owned subsidiary may:

(i) Real estate investment activities. Engage in real estate investment activities. However, the requirements of paragraph (c)(2)(ii), (v), (vi), and (xi) of this section need not be met if the bank's investment in the equity securities of the subsidiary does not exceed 2 percent of the bank's tier one capital; the bank has only one subsidiary engaging in real estate investment activities; and the bank's total investment in the subsidiary does not include any extensions of credit from the bank to the subsidiary, any debt instruments issued by the subsidiary, or any other transaction originated by the bank that is used to benefit the subsidiary.

(ii) Securities activities. Engage in the public sale, distribution or underwriting of securities that are not permissible for a national bank under section 16 of the Banking Act of 1933 (12 U.S.C. 24 Seventh), provided that the insured state nonmember bank lawfully controlled or acquired the subsidiary and had an approved notice or order from the FDIC prior to November 12, 1999 and provided that the following additional conditions are, and continue to be, met:

(A) The state-chartered depository institution adopts policies and procedures, including appropriate limits on exposure, to govern the institution's participation in financing transactions underwritten or arranged by an underwriting majority-owned subsidiary;

(B) The state-chartered depository institution may not express an opinion on the value or the advisability of the purchase or sale of securities underwritten or dealt in by a ma-

jority-owned subsidiary unless the state-chartered depository institution notifies the customer that the majority-owned subsidiary is underwriting or distributing the security;

(C) The majority-owned subsidiary is registered with the Securities and Exchange Commission, is a member in good standing with the appropriate self-regulatory organization, and promptly informs the appropriate regional director (DSC) in writing of any material actions taken against the majority-owned subsidiary or any of its employees by the State, the appropriate self-regulatory organizations or the Securities and Exchange Commission; and

(D) The state-chartered depository institution does not knowingly purchase as principal or fiduciary during the existence of any underwriting or selling syndicate any securities underwritten by the majority-owned subsidiary unless the purchase is approved by the state-chartered depository institution's board of directors before the securities are initially offered for sale to the public.

(6) Real estate leasing. A majority-owned subsidiary of an insured State bank acting as lessor under a real property lease which is the equivalent of a financing transaction, meeting the lease criteria of paragraph (b)(6)(i) of this section and the underlying real estate requirements of paragraph (b)(6)(ii) of this section, does not represent a significant risk to the Deposit Insurance Fund. A majority-owned subsidiary may conduct this activity without first obtaining the FDIC's consent, provided that the bank meets and continues to meet the applicable capital standards as prescribed by the appropriate Federal banking agency. The fact that prior consent is not required by this subpart does not preclude the FDIC from taking any appropriate action with respect to the activity if the facts and circumstances warrant such action.

(i) Lease criteria--

(A) Capital lease. The lease must qualify as a capital lease as to the lessor under generally accepted accounting principles.

(B) Nonoperating basis. The bank and the majority-owned subsidiary shall not, directly or indirectly, provide or be obligated to provide servicing, repair, or maintenance to the property, except that the lease may include provisions permitting the subsidiary to protect the value of the leased property in the event of a change in circumstances that increases the subsidiary's exposure to loss, or the subsidiary may take reasonable and appropriate action to salvage or protect the value of the leased property in such circumstances.

(ii) Underlying real property requirements--

(A) Acquisition. The majority-owned subsidiary may acquire specific real estate to be leased only after the subsidiary has entered into:

(1) A lease meeting the requirements of paragraph (b)(6)(i) of this section;

(2) A legally binding written commitment to enter into such a lease; or

(3) A legally binding written agreement that indemnifies the subsidiary against loss in connection with its acquisition of the property.

(B) Improvements. Any expenditures by the majority-owned subsidiary to make reasonable repairs, renovations, and improvements necessary to render the property suitable to the lessee shall not exceed 25 percent of the majority-owned subsidiary's full investment in the real estate.

(C) Divestiture. At the expiration of the initial lease (including any renewals or extensions thereof), the majority-owned subsidiary shall, as soon as practicable but in any event no less than two years, either:

(1) Re-lease the property under a lease meeting the requirement of paragraph (b)(6)(i)(B) of this section; or

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(2) Divest itself of all interest in the property.

(7) Acquiring and retaining adjustable rate and money market preferred stock and similar instruments. The FDIC has determined it does not present a significant risk to the Deposit Insurance Fund for a majority-owned subsidiary of an insured State bank to engage in any activity permissible for an insured State bank under § 362.3(b)(2)(iii), so long as instruments held under this paragraph, paragraph (b)(3)(ii)(C) of this section, and § 362.3(b)(2)(iii) in the aggregate do not exceed the limit set by § 362.3(b)(2)(iii). A majority-owned subsidiary may conduct this activity without first obtaining the FDIC's consent, provided that the bank meets and continues to meet the applicable capital standards as prescribed by the appropriate Federal banking agency. The fact that prior consent is not required by this subpart does not preclude the FDIC from taking any appropriate action with respect to the activity if the facts and circumstances warrant such action.

(c) Core eligibility requirements. If specifically required by this part or by FDIC order, any state-chartered depository institution that wishes to be eligible and continue to be eligible to conduct as principal activities through a subsidiary that are not permissible for a subsidiary of a national bank must be an “eligible depository institution” and the subsidiary must be an “eligible subsidiary”.

(1) A state-chartered depository institution is an “eligible depository institution” if it:

(i) Has been chartered and operating for three or more years, unless the appropriate regional director (DSC) finds that the state-chartered depository institution is owned by an established, well-capitalized, well-managed holding company or is managed by seasoned management;

(ii) Has an FDIC-assigned composite rating of 1 or 2 assigned under the Uniform Financial Institutions Rating System (UFIRS) (or such other comparable rating system as may be adopted in the future) as a result of its most recent Federal or State examination for which the FDIC assigned a rating;

(iii) Received a rating of 1 or 2 under the “management” component of the UFIRS as assigned by the institution's appropriate Federal banking agency;

(iv) Has a satisfactory or better Community Reinvestment Act rating at its most recent examination conducted by the institution's appropriate Federal banking agency;

(v) Has a compliance rating of 1 or 2 at its most recent examination conducted by the institution's appropriate Federal banking agency; and

(vi) Is not subject to a cease and desist order, consent order, prompt corrective action directive, formal or informal written agreement, or other administrative agreement with its appropriate Federal banking agency or chartering authority.

(2) A subsidiary of a state-chartered depository institution is an “eligible subsidiary” if it:

(i) Meets applicable statutory or regulatory capital requirements and has sufficient operating capital in light of the normal obligations that are reasonably foreseeable for a business of its size and character within the industry;

(ii) Is physically separate and distinct in its operations from the operations of the state-chartered depository institution, provided that this requirement shall not be construed to prohibit the state-chartered depository institution and its subsidiary from sharing the same facility if the area where the subsidiary conducts business with the public is clearly distinct from the area where customers of the state-chartered depository institution conduct business with the institution. The extent of the separation will vary according to the type and frequency of customer contact;

(iii) Maintains separate accounting and other business records;

(iv) Observes separate business entity formalities such as separate board of directors' meetings;

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(v) Has a chief executive officer of the subsidiary who is not an employee of the institution;

(vi) Has a majority of its board of directors who are neither directors nor executive officers of the state-chartered depository institution;

(vii) Conducts business pursuant to independent policies and procedures designed to inform customers and prospective customers of the subsidiary that the subsidiary is a separate organization from the state-chartered depository institution and that the state-chartered depository institution is not responsible for and does not guarantee the obligations of the subsidiary;

(viii) Has only one business purpose within the types described in paragraphs (b)(2) and (b)(5) of this section;

(ix) Has a current written business plan that is appropriate to the type and scope of business conducted by the subsidiary;

(x) Has qualified management and employees for the type of activity contemplated, including all required licenses and memberships, and complies with industry standards; and

(xi) Establishes policies and procedures to ensure adequate computer, audit and accounting systems, internal risk management controls, and has necessary operational and managerial infrastructure to implement the business plan.

(d) Investment and transaction limits--

(1) General. If specifically required by this part or FDIC order, the following conditions and restrictions apply to an insured State bank and its subsidiaries that engage in and wish to continue to engage in activities which are not permissible for a national bank subsidiary.

(2) Investment limits--

(i) Aggregate investment in subsidiaries. An insured state bank's aggregate investment in all subsidiaries conducting activities subject to this paragraph (d) shall not exceed 20 percent of the insured State bank's tier one capital.

(ii) Definition of investment.

(A) For purposes of this paragraph (d), the term “investment” means:

(1) Any extension of credit to the subsidiary by the insured State bank;

(2) Any debt securities, as such term is defined in part 344 of this chapter, issued by the subsidiary held by the insured State bank;

(3) The acceptance by the insured State bank of securities issued by the subsidiary as collateral for an extension of credit to any person or company; and

(4) Any extensions of credit by the insured State bank to any third party for the purpose of making a direct investment in the subsidiary, making any investment in which the subsidiary has an interest, or which is used for the benefit of, or transferred to, the subsidiary.

(B) For the purposes of this paragraph (d), the term “investment” does not include:

(1) Extensions of credit by the insured State bank to finance sales of assets by the subsidiary which do not involve more than the normal degree of risk of repayment and are extended on terms that are substantially similar to those prevailing at the time for comparable transactions with or involving unaffiliated persons or companies;

(2) An extension of credit by the insured State bank to the subsidiary that is fully collateralized by government securities, as such term is defined in § 344.3 of this chapter; or

(3) An extension of credit by the insured State bank to the subsidiary that is

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fully collateralized by a segregated deposit in the insured State bank.

(3) Transaction requirements--

(i) Arm's length transaction requirement. With the exception of giving the subsidiary immediate credit for uncollected items received in the ordinary course of business, an insured State bank may not carry out any of the following transactions with a subsidiary subject to this paragraph (d) unless the transaction is on terms and conditions that are substantially the same as those prevailing at the time for comparable transactions with unaffiliated parties:

(A) Make an investment in the subsidiary;

(B) Purchase from or sell to the subsidiary any assets (including securities);

(C) Enter into a contract, lease, or other type of agreement with the subsidiary;

(D) Pay compensation to a majority-owned subsidiary or any person or company who has an interest in the subsidiary; or

(E) Engage in any such transaction in which the proceeds thereof are used for the benefit of, or are transferred to, the subsidiary.

(ii) Prohibition on purchase of low quality assets. An insured State bank is prohibited from purchasing a low quality asset from a subsidiary subject to this paragraph (d). For purposes of this subsection, "low quality asset" means:

(A) An asset classified as "substandard", "doubtful", or "loss" or treated as "other assets especially mentioned" in the most recent report of examination of the bank;

(B) An asset in a nonaccrual status;

(C) An asset on which principal or interest payments are more than 30 days past due; or

(D) An asset whose terms have been renegotiated or compromised due to the deteriorating financial condition of the obligor.

(iii) Insider transaction restriction. Neither the insured State bank nor the subsidiary subject to this paragraph (d) may enter into any transaction (exclusive of those covered by § 337.3 of this chapter) with the bank's executive officers, directors, principal shareholders or related interests of such persons which relate to the subsidiary's activities unless:

(A) The transactions are on terms and conditions that are substantially the same as those prevailing at the time for comparable transactions with persons not affiliated with the insured State bank; or

(B) The transactions are pursuant to a benefit or compensation program that is widely available to employees of the bank, and that does not give preference to the bank's executive officers, directors, principal shareholders or related interests of such persons over other bank employees.

(iv) Anti-tying restriction. Neither the insured State bank nor the majority-owned subsidiary may require a customer to either buy any product or use any service from the other as a condition of entering into a transaction.

(4) Collateralization requirements.

(i) An insured State bank is prohibited from making an investment in a subsidiary subject to this paragraph (d) unless such transaction is fully-collateralized at the time the transaction is entered into. No insured State bank may accept a low quality asset as collateral. An extension of credit is fully collateralized if it is secured at the time of the transaction by collateral having a market value equal to at least:

(A) 100 percent of the amount of the transaction if the collateral is composed of:

(1) Obligations of the United States or its agencies;

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(2) Obligations fully guaranteed by the United States or its agencies as to principal and interest;

(3) Notes, drafts, bills of exchange or bankers acceptances that are eligible for rediscount or purchase by the Federal Reserve Bank; or

(4) A segregated, earmarked deposit account with the insured State bank;

(B) 110 percent of the amount of the transaction if the collateral is composed of obligations of any State or political subdivision of any State;

(C) 120 percent of the amount of the transaction if the collateral is composed of other debt instruments, including receivables; or

(D) 130 percent of the amount of the transaction if the collateral is composed of stock, leases, or other real or personal property.

(ii) An insured State bank may not release collateral prior to proportional payment of the extension of credit; however, collateral may be substituted if there is no diminution of collateral coverage.

(5) Investment and transaction limits extended to insured State bank subsidiaries. For purposes of applying paragraphs (d)(2) through (d)(4) of this section, any reference to "insured State bank" means the insured State bank and any subsidiaries of the insured State bank which are not themselves subject under this part or FDIC order to the restrictions of this paragraph (d).

(e) Capital requirements. If specifically required by this part or by FDIC order, any insured State bank that wishes to conduct or continue to conduct as principal activities through a subsidiary that are not permissible for a subsidiary of a national bank must:

(1) Be well-capitalized after deducting from its tier one capital the investment in equity securities of the subsidiary as well as the bank's pro rata share of any retained earnings of the subsidiary;

(2) Reflect this deduction on the appropriate schedule of the bank's consolidated report of income and condition; and

(3) Use such regulatory capital amount for the purposes of the bank's assessment risk classification under part 327 of this chapter and its categorization as a "well-capitalized", an "adequately capitalized", an "undercapitalized", or a "significantly undercapitalized" institution as defined in § 325.103(b) of this chapter, provided that the capital deduction shall not be used for purposes of determining whether the bank is "critically undercapitalized" under part 325 of this chapter.

[66 FR 1028, Jan. 5, 2001; 71 FR 20527, April 21, 2006]

SOURCE: 63 FR 66326, Dec. 1, 1998; 65 FR 15530, March 23, 2000; 66 FR 1028, Jan. 5, 2001, unless otherwise noted.

AUTHORITY: 12 U.S.C. 1816, 1818, 1819(a) (Tenth), 1828(j), 1828(m), 1828a, 1831a, 1831e, 1831w, 1843(l).

12 C. F. R. § 362.4, 12 CFR § 362.4

Current through November 25, 2009; 74 FR 62188

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2004 WL 2191294 (O.C.C.)

Office of the Comptroller of the Currency (O.C.C.)

***1** Interpretive Letter No. 1007

Interpretive Letter No. 1007

September 7, 2004

Re: **[***]** ("Bank")
Dear **[***]**:
We understand that the Bank owns **[*ABC*]** corporate debt and holds it as a Type III investment security. As part of **[*ABC*]**'s bankruptcy reorganization plan, all holders of that particular issue will be required to exchange their debt for an equity interest in **[*Co.*]**, *i.e.*, stock, or for debt that would not qualify as an investment security, due to its below-investment grade rating. We have been asked whether it is permissible for the Bank to accept **[*Co.*]** equity or below-investment grade debt in an exchange for **[*ABC*]** debt, on the theory that the bank would accept the securities as an exercise of its power to take bank-impermissible property in satisfaction of debt previously contracted ("DPC"). For the reasons discussed below, we conclude that the Bank may accept **[*Co.*]** equity or below-investment grade debt in an exchange for **[*ABC*]** debt.

Background
As we understand the facts, the Bank held **[*ABC*]** corporate debt as a Type III investment security under its authority to purchase and hold investment securities. As part of **[*ABC*]**'s bankruptcy reorganization plan, all holders of that particular issue will be required to exchange their debt for an equity interest in **[*Co.*]**, *i.e.*, stock, or for debt that would not qualify as an investment security, due to its below investment grade rating.

Law
The ability of a national bank to take DPC property is an extension of a national bank's authority to make loans. A national bank may negotiate directly with a borrower to extinguish a poor quality credit in exchange for some form of property, including assets the bank otherwise is not permitted to own or hold, such as real estate and corporate stock, so that the bank may obtain a better recovery through the acceptance and later sale of property than through holding the loan. National banks may acquire and hold equity securities in order to improve the prospects for recovery on loans that are in default, are nonperforming, or otherwise have a history of poor performance. In certain circumstances and subject to limitations, national banks can invest additional cash to improve DPC property and increase ultimate recoveries.[FN1]

There is explicit authority for national banks to take and hold real estate in satisfaction of DPC.[FN2] The ability to take and hold other DPC property is incidental to a national bank's authority to lend.[FN3] National banks also may purchase and hold debt securities as an exercise of their lending authority.[FN4]

National banks may not use their DPC authority as a means of speculation[FN5] and cannot hold DPC property indefinitely. National banks must dispose of the property within five years, with the opportunity to apply to extend the holding period for an additional five years.[FN6] Congress recognized this authority, in effect, in placing a time limitation on a national bank's holding of real estate obtained in satisfaction of debt previously contracted.[FN7] The OCC

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has applied the five-plus-five holding period limitation to other forms of property as well.[FN8]

***2** The OCC's regulation governing national bank investment in investment securities, 12 C.F.R. Part 1, recognizes the ability of national banks to use DPC authority to convert or exchange holdings of non-performing investment securities into stock or other bank-impermissible property.[FN9] Section 1.7 states that, with three exceptions, the restrictions and limitations of Part 1 do not apply to securities acquired through foreclosures on collateral, in good faith by way of compromise of a doubtful claim, or to avoid loss in connection with a debt previously contracted.[FN10] A national bank may hold securities acquired in satisfaction of debt previously contracted ("DPC securities") for no more than five years, with a possible five year extension, shall account for DPC securities in accordance with Generally Accepted Accounting Principles, and may not hold DPC securities for speculative purposes.[FN11]

Discussion

When a national bank exercises its lending authority, regardless of the legal form that the extension of credit takes, the bank should be able to use its DPC authority when a credit event warrants. A bank may exercise its lending authority, for example, by taking a note directly from a borrower collateralized by securities, or by buying debt securities in the market. In the latter case, if the security loses its value due to the issuer's failure to perform, the bank should be able to exchange the security for DPC property in a DPC transaction. It would be anomalous to deny a bank this authority for an asset acquired under the authority to lend, simply because the asset takes the form of a security. OCC precedent makes clear that a national bank acquiring a security under its lending authority must observe a variety of restrictions applicable to the making and administration of loans, and without specifically denying the authority to engage in DPC transactions with respect to those assets.[FN12]

DPC theory does not necessarily limit itself conceptually only to situations involving the exercise of lending authority. National banks may acquire assets through a variety of authorities other than the authority to make loans, and those acquisitions, when made in good faith, can result in impairment of values due to credit events, just as in the case of a loan. If it is incidental to a bank's authority to lend to acquire bank-impermissible property to improve the prospects of recovery on an impaired loan, that analysis is equally valid in the case of another impaired asset the bank has acquired under separate authority. It is anomalous to permit a national bank the ability to exchange a non-performing asset in a DPC transaction when the bank acquired that asset using its lending authority, and simultaneously deny the bank the authority to engage in an identical DPC transaction, simply because the economically identical asset originally was acquired under a different authority.

National banks may use DPC authority to protect their interests in resolving a troubled credit relationship, regardless of whether the bank acquired the asset using its authority to lend or purchase and hold investment securities. National banks may use DPC authority to exchange investment securities in DPC transactions for securities that are otherwise not permissible for investment where the banks clearly establish the need to protect their interest in a troubled credit relationship. Banks must be able to demonstrate that any instruments acquired using DPC authority were taken to resolve a troubled credit situation in which the bank otherwise would face credit losses. Accordingly, a national bank may rely on its authority to take otherwise impermissible securities in DPC transactions, in cases of settlements offered through bankruptcy proceedings. In this case, as part of **[*ABC*]**'s bankruptcy reorganization plan, all holders of **[*ABC*]** debt will be required to exchange their debt for an equity interest in **[*Co.*]**, *i.e.*, stock, or for debt that would not qualify as an investment security, due to its below investment grade rating. Taking the equity security or below-investment grade debt is the only option the Bank has to recover on the troubled debt situation.

Conclusion

***3** We conclude that in the context of the **[*ABC*]** bankruptcy reorganization plan established by the bankruptcy court, it is permissible for the Bank to accept **[*Co.*]** equity or below-investment grade debt in an exchange for **[*ABC*]** debt, on the theory that the bank would accept the securities as an exercise of its power to take bank-impermissible property in satisfaction of DPC.

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Sincerely,

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First Senior Deputy Comptroller and Chief Counsel

FN1. *See* *First National Bank of Charlotte v. National Exchange Bank of Baltimore*, 92 U.S. 122, 127 (1875), and *Atherton v. Anderson*, 86 F.2d 518, 525 (6th Cir. 1936), *rev'd on other grounds*, 302 U.S. 643 (1937).

FN2. Under 12 U.S.C. 29 (Third), a national bank may "purchase, hold, and convey real estate . . . such as shall be conveyed to it in satisfaction of debts previously contracted in the course of its dealings."

FN3. *See* 12 U.S.C. 24 (Seventh) and OCC Interpretive Letter No. 643 (July1, 1992), *reprinted in* [1994 Transfer Binder] Fed. Banking L. Rep. (CCH) 83,551.

FN4. *See, e.g.,* OCC Interpretive Letter No. 908 (Apr. 23, 2001), *Interpretations and Actions* (May 2001). Banks that acquire securities under their lending authority must observe a number of rules and restrictions that apply to the making and administration of loans, such as underwriting standards and the lending limit, found at 12 U.S.C. 84

FN5. *See* OCC No-Objection Letter No. 89-01 (Jan. 25, 1989), *reprinted in* [1988-89 Transfer Binder] Fed. Banking L. Rep. (CCH) 83,009.

FN6. *See* 12 U.S.C. 29(Third).

FN7. *See* 12 U.S.C. 29(Third).

FN8. *See* OCC Interpretive Letter No. 643, *supra*.

FN9. *See* 12 C.F.R. 1.7.

FN10. *See* 12 C.F.R. 1.7(a)(1)-(3).

FN11. *See* 12 C.F.R. 1.7(b)-(d).

FN12. *See* Interpretive Letter No. 908, *supra*. This precedent details the obligation of a national bank to observe various legal requirements relating to the holding of securities that were acquired under lending authority, but does not address whether the bank may effect a DPC transaction in the event of a credit-related impairment of those assets.

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General Information

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