Office of Thrift Supervision
Department of the Treasury
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LEGAL OPINION

TO: John F. Downey
Director of Supervision

FROM: Business Transactions Division

SUBJECT: Application by [redacted] (the "Purchasing Association") and [redacted] (which is to be renamed [redacted] FSB) (the "Selling Association") for the Purchase of Certain Assets and the Assumption of Certain Liabilities

DATE: May 5, 1995

I. INTRODUCTION AND SUMMARY CONCLUSION

[redacted] (the "Holding Company"), is a registered savings and loan holding company with two wholly-owned savings association subsidiaries, the Purchasing Association and the Selling Association (jointly referred to as the "Applicants"). The Applicants have filed an application seeking the approval of the Office of Thrift Supervision ("OTS"), under 12 U.S.C. § 1828(c) of the Federal Deposit Insurance Act (the "FDIA") (the "Bank Merger Act" or "BMA") and 12 C.F.R. § 563.22, for the proposed purchase of certain assets and the proposed assumption of certain liabilities of the Selling Association by the Purchasing Association. The Selling Association will modify its business plan to provide certain financial services on the Internet, a worldwide computer network.

The [redacted] Regional Office (the "Regional Office"), Compliance Policy, and Corporate Activities have reviewed the application and have recommended approval of the application, subject to three conditions designed to ensure that the Applicants continue to satisfy their Community Reinvestment Act obligations, and a condition designed to ensure the security of the Selling Association's computer system. We have reviewed the application under applicable statutes and regulations and have no legal objection to approval of the application, subject to the standard conditions and the non-standard conditions recommended.

II. BACKGROUND

A. The Parties

1. The Holding Company

The Holding Company is a registered bank holding company and a registered savings and loan holding company. The Holding Company's business operations are conducted primarily through its three bank subsidiaries and its two thrift subsidiaries, the Applicants. As of December 31, 1994, the Holding Company had total assets of [redacted] and total stockholders' equity of [redacted] on a consolidated basis.

2. The Purchasing Association

The Purchasing Association, a SAIF-insured federal stock savings bank and a wholly owned direct subsidiary of the Holding Company, has its home office in [redacted], and has [redacted] branch offices in [redacted]. As of December 31, 1994, the Purchasing Association had total assets of [redacted] tangible and core capital ratios of [redacted] and a risk-based capital ratio of [redacted]. At its most recent examination, the Purchasing Association received a composite CAMEL rating of [redacted], a compliance rating of [redacted] and a Community Reinvestment Act ("CRA") rating of "Satisfactory."

3. The Selling Association

The Selling Association, a SAIF-insured federal stock savings bank and a wholly owned direct subsidiary of the Holding Company, has its home office in [redacted] and has [redacted] branch offices. As of December 31, 1994, the Selling Association had total assets of [redacted] tangible and core capital ratios of [redacted] and a risk-based capital ratio of [redacted]. At its most recent examination, the Selling Association received a composite CAMEL rating of [redacted], a compliance rating of [redacted] and a CRA rating of "Satisfactory."

B. The Proposed Transaction

The proposed transaction provides for the purchase of certain assets of the Selling Association (including its four branch offices) by the Purchasing Association and the assumption of certain liabilities of the Selling Association (including the liabilities for deposit and savings accounts at the four branches) by the Purchasing Association. However, the Selling Association will retain certain assets (including its home office) and certain liabilities (including the liabilities for deposit and savings accounts at the home office). See the [redacted] Regional Digest, dated April 11, 1995 (the "Regional Digest"), at page 2, for a description of the assets and liabilities to be retained. Upon consummation of the proposed transaction, the Purchasing

Association will have total assets of [redacted], tangible and core capital ratios of [redacted] and a risk-based capital ratio of [redacted] and the Selling Association will have total assets of [redacted] million, equity capital of [redacted] million, tangible and core capital ratios of [redacted] and a risk-based capital ratio of [redacted]

Following consummation of the proposed transaction, the Selling Association intends to deliver certain financial services through the Internet, a worldwide computer network, and through its community office. For a description of the financial services to be offered through the Internet, see the Regional Digest, at pages 2 through 4, and Exhibit 3, which is attached to the Regional Digest.

III. DISCUSSION

A. Merger Application

The Regional Office and CA have reviewed the application and have recommended approval. We have reviewed the proposed transfer of assets and assumption of liabilities under the BHA and the OTS merger regulations,[1] and have no legal objection to approval, subject to the standard conditions and the non-standard conditions recommended by the Regional Office.

Pursuant to the BHA and OTS regulations thereunder, the OTS must take into consideration the financial and managerial resources and future prospects of the existing and proposed institutions, and the convenience and needs of the community to be served.[2] In addition, the OTS must consider the impact of the transaction on competition, and is required to deny the application under certain circumstances.[3]

The Regional Office has not objected to the managerial and financial resources and future prospects of the resulting institutions. The Regional Digest indicates that following the proposed transaction both the Purchasing Association and the Selling Association will satisfy their regulatory capital requirements.

In addition, the Regional Office and Corporate Activities have reviewed the business plan submitted by the Selling Association, and have found the business plan to be acceptable. In order to ensure the security of the Selling Association's computer system, the Regional Office has recommended a condition requiring that the Selling Association cause independent tests of the functionality and security of its operations to be performed

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1. 12 U.S.C. § 1828(c), and 12 C.F.R. § 563.22 (1995).

2. 12 U.S.C. § 1828(c)(5); 12 C.F.R. § 563.22(d) (1995).

3. Id.

before and after implementation of the computer system. The condition requires that the tests confirm in writing that the computer system does not allow unauthorized or undetected access to customer accounts, with reasonable certainty.

Based on the conclusions of the Regional Office and Corporate Activities, we have no legal objection to approval based on the managerial and financial resources and future prospects of the Applicants. We have no objection to the non-standard condition recommended by the Regional Office.

In our opinion, the proposed transaction is not objectionable on antitrust grounds, because both the Purchasing Association and the Selling Association will continue to be wholly-owned subsidiaries of the Holding Company. Pursuant to the BHA, the OTS staff requested reports from the United States Department of Justice ("DOJ") and the other federal banking regulators analyzing the competitive factors in the proposed transaction. The DOJ advised the OTS that the transaction would not have a significant adverse effect on competition and the other federal banking regulators have not objected to the transaction.

With respect to the CRA and the convenience and needs of the community, the Purchasing Association and the Selling Association both received satisfactory CRA ratings in their most recent compliance examinations. The OTS has received no protests or other comments relating to the convenience and needs of the communities served in response to the public notice regarding the proposed transaction.

In connection with OTS review of the application, Compliance Policy attempted to confirm how the Selling Association would use its expanded Internet deposit base to help meet the credit needs of its community, and asked for elaboration of the Purchasing Association's plans for its expanded community. Compliance Policy's memorandum mentions certain initiatives that have been undertaken by the Applicants in this area.

Based on the Applicants' satisfactory CRA ratings, and their new initiatives (which were not fully implemented as of the date of Compliance Policy's memorandum), Compliance Policy has not objected to the proposed transaction on the basis of either the CRA or the convenience and needs of the communities to be served. However, Compliance Policy and the Regional Office have recommended three CRA-related non-standard conditions. See the Regional Digest, at page 13, and Compliance Policy's memorandum. We have no legal objection to imposition of the conditions.

B. Transactions With Affiliates Issues

The proposed transaction involving the Purchasing Association and the Selling Association is not subject to the limitations on transaction with affiliates set forth at section 23A of the Federal Reserve Act ("FRA").[4] Section 250.241(a) of the regulations of the Board of Governors of the Federal Reserve System provides that section 23A of the FRA shall not apply to a transaction between affiliated insured depository institutions if the transaction has been approved by the appropriate federal banking agency pursuant to the BHA.[5]

Nevertheless, the proposed transaction is subject to the provisions of section 23B of the FRA and OTS regulations thereunder.[6] Accordingly, the proposed transaction must be conducted on terms and under circumstances that are substantially the same, or at least as favorable to the association as those prevailing at the time for comparable transactions involving nonaffiliated companies. We defer to Corporate Activities to

4. 12 U.S.C. § 371c.

5. 12 C.F.R. § 250.241(a) (1995). The Regional Office's digest states that the Selling Association is not transferring its home office to the Purchasing Association because the Selling Association's low-quality assets cannot be transferred to the Purchasing Association. See 12 U.S.C. § 371c(d); 12 C.F.R. § 563.43(d) (1995). We note that such a transfer would not be prohibited, given that 12 C.F.R. § 250.241 exempts the transaction from section 23A of the FRA.

6. 12 U.S.C. § 371c-1; 12 C.F.R. § 563.42 (1995).

advise the Director of Supervision as to whether the proposed transaction meets this standard.[7]

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7. 12 U.S.C. § 371c-1(a)(1); 12 C.F.R. § 563.42(a) (1995).