UNITED STATES OF AMERICA
Before the
OFFICE OF THRIFT SUPERVISION
OF THE DEPARTMENT OF THE TREASURY

In the Matter of: CHARLES H. KEATING, JR., JUDY J. WISCHER, ROBERT J. KIELTY, CHARLES H. KEATING, III, ROBERT J. HUBBARD, JR., ROBERT M. WURZELBACHER, JR. ANDRE NIEBLING, Former Directors of American Continental Corporation, the Savings and Loan Holding Company of Lincoln Savings and Loan Association, Irvine, California	Order No. 90-1464 dated August 9, 1990 as amended by Order No. 91-4 dated January 29, 1991 OTS Order No. AP 93-85 Dated: October 22, 1993

FINAL DECISION AND ORDER

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DECISION

I. INTRODUCTION AND SUMMARY OF CONCLUSIONS

The failure of Lincoln Savings and Loan Association, Irvine, California ("Lincoln"), which will cost the taxpayers an estimated $2.6 billion, resulted in large measure from insider abuses, including those that are the subject of this enforcement proceeding. Lincoln was the wholly owned subsidiary of its holding company, American Continental Corporation ("ACC").[1]

Charles H. Keating, Jr. ("Keating" or "Respondent") was the Chairman of the Board and controlling shareholder of ACC at all relevant times, and he was also President and Chief Executive Officer of ACC from September 1981 through May 1985. Keating's domination of the holding company enabled him to control Lincoln and use it -- and its federal deposit insurance guarantee -- as if it were his private coffer.

In the matter before the Acting Director, the Special Trial Division ("Enforcement Counsel") of the Office of Thrift Supervision ("OTS") seeks an order against Keating to cease and desist and directing restitution and an order of prohibition based

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1. ACC filed for protection under Chapter 11 of the United States Bankruptcy Code, 11 U.S.C. § 1101 et seq., on April 13, 1989. On April 14, 1989, Lincoln was placed into conservatorship by the Federal Home Loan Bank Board ("FHLBB"). On August 2, 1989, the FHLBB appointed a receiver for Lincoln.

on two transactions evidencing egregious insider abuse.[2] The record conclusively demonstrates that Keating deliberately manipulated Lincoln for his personal financial benefit in defiance of his fiduciary responsibilities and with a disregard for the law and for the institution's safety and soundness.

First, Keating personally and, in combination with others, caused certain Lincoln subsidiaries to loan funds to the Hotel Pontchartrain Limited Partnership ("HPLP") on terms disastrous for the lenders. HPLP was a tax shelter in which Keating, his immediate family and other officers and directors of ACC, Lincoln, and its subsidiaries were limited partners. The subsequent failure of HPLP to repay the loan resulted in losses to Lincoln of approximately $24.2 million.

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2. The Amended Notice of Charges and Hearing to Direct Restitution and Notice of Intention to Remove and Prohibit Respondents from Participation in the affairs of Federally Insured Institutions issued January 29, 1991 ("Amended Notice") named seven respondents: Keating, Robert J. Kielty ("Kielty"), Charles H. Keating, III ("Keating III"), Robert J. Hubbard, Jr. ("Hubbard"), Judy J. Wischer ("Wischer"), Robert M. Wurzelbacher, Jr. ("Wurzelbacher") and Andre Niebling ("Niebling").

The Director entered into stipulations with Wischer, Hubbard, Niebling, Wurzelbacher, Keating III and Kielty, in which each of these respondents, without admitting or denying the assertions made in the Amended Notice, consented to the issuance of an order that would prohibit each respondent from participating in the affairs of federally insured depository institutions. By each stipulation the consenting respondent waived his or her right to an administrative hearing, and each consented to issuance of an order requiring him or her to cease and desist from committing or aiding and abetting the commission of unsafe and unsound practices and violations of law, rules and regulations set forth in the Amended Notice of Charges. See OTS Order Nos. AP 92-79-82 (August 14, 1992) (Wurzelbacher, Wischer, Hubbard and Niebling, respectively), OTS Order No. AP 92-89 (September 3, 1992) (Keating III) and OTS Order No. AP 93-63 (July 16, 1993) (Kielty).

Second, motivated by his desire to sell his ACC stock, Keating directed officers and directors of ACC and Lincoln to cause an Employee Stock Ownership Plan established for the benefit of ACC and Lincoln employees (the "ESOP") to borrow $20 million. An essential element of the transaction was Lincoln's pledge of assets and guarantee of $15 million of the ESOP's debt. ACC, however, appointed the ESOP's Trustee, and ACC and Keating controlled the Administrative Committee that was responsible for making decisions on behalf of the ESOP. The ESOP used the proceeds of the loan to purchase ACC stock from insiders. When the ESOP defaulted on its obligations following ACC's bankruptcy, Lincoln lost approximately $12.2 million.

The Acting Director finds that Keating violated law and regulations prohibiting transactions with affiliates and affiliated persons; that he engaged in unsafe and unsound practices; and that he breached his fiduciary duties as a controlling shareholder of Lincoln, including engaging in prohibited conflicts of interest. Respondent was unjustly enriched by his conduct: he realized $700,000 in tax savings by recording losses from HPLP, and he was paid $1.65 million for his stock in ACC by the ESOP with the proceeds of the ESOP's borrowing. Lincoln itself suffered losses of over $36 million on the HPLP and ESOP transactions.

Keating's conduct involved reckless disregard for banking laws and regulations, willful and continuing disregard for the safety and soundness of Lincoln, and conclusively demonstrates his unfitness to participate in the conduct of the affairs of Lincoln or any other depository institution. Based on the administrative record and the applicable statutory standards, the Acting Director concludes that a cease and desist order requiring restitution of $36,398,738.76 and a prohibition order should issue against Respondent.[3]

II. BACKGROUND

A. Summary of Administrative Proceedings

On August 9, 1990, the OTS issued a Notice of Charges and Hearing to Direct Restitution and Notice of Intention to Remove and Prohibit Respondents from Participation in the Affairs of Federally Insured Institutions ("Notice of Charges") against Respondent and others. On January 29, 1991, the OTS issued an Amended Notice.[4] The Amended Notice alleges, inter alia, that Respondent engaged in numerous unsafe and unsound practices; violated regulations and statutes, including 12 C.F.R. sections 563.43, 584.3, 563.23-3

3. An order of removal is unnecessary since Respondent no longer holds any position with Lincoln or ACC. See In the Matter of Keating, Decision and Order on Respondents' Motion to Dismiss, OTS Order No. AP 91-20 (May 13, 1991) at 7, n.5.

4. The Amended Notice added Niebling as a respondent, added charges relating to a tax sharing agreement, and made other modifications and clarifications to the Notice of Charges.

(1985);[5] and Respondent violated his fiduciary duties to Lincoln as a controlling shareholder of the institution, including engaging in impermissible conflicts of interest relating to the HPLP and the ESOP transactions.[6] The Amended Notice seeks an order to cease and desist and directing restitution and an order of removal and prohibition.

Respondent timely filed answers to the Notice of Charges and the Amended Notice. A hearing was conducted by the ALJ on July 1 through 3 and 8 through 12, 1991, in Los Angeles, California. The hearing continued on April 27 through May 1, 1992, in Phoenix,

5. Several of the regulations at issue in this proceeding have been amended since the conduct at issue occurred. Citations are to the regulations in effect during the relevant time period.

6. This Decision and Order covers only two of the four transactions alleged as grounds for the remedies sought in the Amended Notice. By Order dated March 24, 1992, the Administrative Law Judge ("ALJ") severed the charges relating to the other two transactions -- the Westcontinental Land Sale and the Tax Sharing Agreement between Lincoln and ACC -- from the charges addressed herein because they were the subject of then pending criminal cases against certain of the respondents named in the Amended Notice, including Keating.

On December 4, 1991, Keating was convicted of criminal securities fraud in a trial in the California Superior Court. People v. Keating, Case No. BA 025236 (affirmed on appeal, B067329 (June 3, 1993)). As a result of this conviction, Respondent has been sentenced to 10 years in prison, and ordered to pay $250,000 in criminal fines. On January 6, 1993, Respondent was convicted on counts of racketeering, conspiracy and fraud in a federal trial in the United States District Court for the Central District of California. United States v. Keating, No. CR 91-1021-MRP (C.D. Cal. January 6, 1993) (appeal pending). As a result of this federal conviction, Respondent has been sentenced to 12 1/2 years in federal prison.

Arizona. Respondent appeared through counsel at the hearing.[7] Respondent asserted his rights under the Fifth Amendment to the Constitution against self-incrimination and declined to testify when called as a witness by Enforcement Counsel. Respondent did not put on evidence at the hearing.

On November 23, 1992, Enforcement Counsel filed proposed findings of fact and conclusions of law. Respondent did not file proposed findings or conclusions, nor did he respond to Enforcement Counsel's filing.

The ALJ's Recommended Decision and Recommended Order ("ALJ's Recommended Decision") were served on the parties on March 15, 1993. Respondent filed exceptions to the ALJ's Recommended Decision on April 14, 1993.[8] On May 4, 1993, Enforcement Counsel filed a response to Respondent's exceptions. On May 13, 1993,

7. Counsel for Respondent was present at the hearing and cross-examined Enforcement Counsel's witnesses at the July phase of the hearing. Respondent's counsel was not present at the April/May, 1992, phase of the hearing except when Respondent took the witness stand. On June 17, 1993, the Acting Director granted Kirkland & Ellis' request to withdraw as counsel for Respondent in the administrative proceeding. OTS Order No. AP 93-47 (June 17, 1993).

8. Respondent's exceptions that are not specifically addressed in this Decision are denied. Respondent excepted generally to all findings of fact and conclusions of law in the ALJ's Recommended Decision. Respondent's failure to clearly identify issues for review constitutes a waiver of objection under 12 C.F.R. § 509.29(b) (1991). However, the Acting Director has reviewed the entire record in the proceeding and finds that the Recommended Decision is supported by the record and applicable law. Therefore, Respondent's objections contained in these general exceptions to all findings of fact and conclusions of law are denied.

Respondent filed a reply to Enforcement Counsel's response.[9] On July 6, 1993, the parties were notified that the record had been submitted to the Acting Director for final decision. On October 4, 1993, the deadline for the Acting Director's final decision was extended until October 22, 1993. OTS Order No. AP 93-78 (October 4, 1993).

B. Summary of the Facts

The Acting Director adopts the ALJ's Findings of Fact, the full text of which is attached as Appendix A to the ALJ's Recommended Decision. The key features of the transactions at issue and Keating's participation in them are summarized below.

1. Keating's Domination of Lincoln

The ALJ determined that Keating dominated, controlled and supervised Lincoln and its subsidiaries. Keating was a controlling shareholder of ACC, and ACC controlled the election of the Directors of Lincoln and, until April 14, 1989, exercised a controlling influence over the management and policies of Lincoln.[10] The ALJ also found that: the Lincoln Board of Directors reported directly to Keating; Keating made proposals to Lincoln's Board of

9. On June 10, 1993, the OTS requested that the parties review indices of the record for accuracy and completeness. On June 17, 1993, Respondent requested a 60-day extension of time within which to respond, which the Acting Director denied. OTS Order No. AP 93-54 (July 2, 1993).

10. ALJ's Findings of Fact ¶ 2 ("Findings ¶__").

Directors regarding the selection and replacement of Directors; Keating, as "leader" of ACC, took an "extreme" interest in Lincoln and its subsidiaries and had a "large say" in what Lincoln did; Keating originated an inordinate amount of business for Lincoln himself; and Keating was very involved in and exercised control over many of the operations of Lincoln and its subsidiaries. The record shows that Keating not only had ultimate control of Lincoln's voting stock through his control of ACC's stock, but in fact Keating had the power to decide what Lincoln's subsidiaries would or would not do, whether or not he was an officer or director of those companies.[11]

2. The HPLP Transaction

The Crescent Hotel Group of Michigan ("CHG/M") was a subsidiary of Lincoln. On December 31, 1984, at Keating's direction, CHG/M purchased the Hotel Pontchartrain ("Hotel") from the Pontchartrain Hotel Co. for $19.5 million. Almost immediately after the acquisition of the Hotel by CHG/M, Keating directed ACC employees to form a limited partnership to purchase the Hotel by the end of the first quarter of 1985. Three months later, on March 31, 1985, CHG/M sold the Hotel to HPLP, the limited partnership formed per Keating's instructions. CHG/M was the general partner of HPLP. Keating, who was a "controlling person" with respect to both ACC and Lincoln, was a limited partner in HPLP and owned 7.92

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11. Enforcement Counsel's Hearing Ex. I-114 at 11-12, 16-17, 71, 77 ("H.Ex. ___"); Transcript of Proceeding at 2976-78, 2989 (Warnicke) ("Transcript at ___ ([name of witness])").

percent of the limited partnership. Keating and other officers and directors of Lincoln and its subsidiaries collectively owned 35.7 percent of HPLP.

Lincoln, under Keating's direction, engaged in a convoluted scheme to finance the purchase of the Hotel by HPLP. The transaction was structured in two parts. First, on December 31, 1984, the Hotel was sold to CHG/M, with a Lincoln subsidiary providing the financing. CHG/M then sold the Hotel to HPLP on March 31, 1985. The reason for this bifurcated structure was to avoid a loan directly from Lincoln or its subsidiaries to HPLP, in an attempt to evade regulations restricting loans to affiliated persons.

During 1985 through 1986, despite heavy losses by the Hotel, CHG/M advanced approximately $10.4 million to HPLP to cover the Hotel's operating losses. There was no documentation whatsoever to support these advances, not even a Note. Had CHG/M not made the advances, HPLP would have defaulted on its mortgage (held by another unrelated institution), the Hotel would have been foreclosed upon, and the HPLP limited partners, including Keating, may have lost their investment. Lincoln and its subsidiaries would not have incurred any losses.

In December 1986, the Phoenician Financial Corporation ("PFC"), another Lincoln subsidiary, granted an unsecured $20 million line of credit to HPLP. This extension of credit was used, in part, to pay off the $10.4 million in advances made by CHG/M and to provide an additional source of funds to cover future operating losses. Thus, Keating protected his personal financial interests at the expense of Lincoln's business interests.

The line of credit was granted despite continuing heavy losses by the Hotel. The line of credit also was unsecured, and, after taking account of a $35 million first mortgage on the Hotel, was $11 million in excess of the Hotel's value. Additionally, the preferential terms of the line of credit -- it was unsecured and bore an interest rate of 10 percent per annum with no payments of principal or interest due for 5 years -- "made it virtually a gift of assets."[12]

Limited partners of HPLP who derived a benefit from the advance and extension of credit included officers and directors of Lincoln who either were, or should have been, involved in the loan approval process. Even the documents authorizing the line of credit were executed by Lincoln officers who were also investors in HPLP. When questioned at the April/May 1992 administrative enforcement hearing about the HPLP transaction, Respondent asserted his Fifth Amendment privilege against self-incrimination and

12. Recommended Decision at 40. ACC's and Lincoln's own law firm, Kaye, Scholer, Fierman, Hays, and Handler ("Kaye Scholer"), strongly criticized the $20 million line of credit in a February 17, 1988 memorandum. Kaye Scholer found that the loan file contained no loan underwriting, financial statements, credit reports, tax returns, or other documents normally required for a loan. In addition, the line of credit was not approved by the Board of Directors of either Lincoln or PFC.

refused to testify when asked if he directed CHG/M, a Lincoln subsidiary, to advance $10.4 million to HPLP and if he directed PFC, another Lincoln subsidiary, to extend a $20 million line of credit to HPLP.[13]

By February 1989, HPLP had drawn approximately $19.5 million on the line of credit. Ultimately, HPLP defaulted on its first mortgage, and on January 2, 1990, the holder of the first mortgage sold the Hotel at a foreclosure sale. None of the $19.5 million was repaid, and unpaid interest by July 31, 1989 amounted to $4.7 million. In total, Lincoln suffered losses of approximately $24.2 million resulting from the line of credit to HPLP.

By virtue of his interest in HPLP, Keating realized tax savings of $700,000 for the tax years 1985-1989. The tax savings realized collectively by insiders of Lincoln and ACC who invested in HPLP were between $2.2 and $2.4 million.

3. The ESOP Transaction

The ESOP was created by the Board of Directors of ACC on December 20, 1984. Under the ESOP plan documents, the ACC Board of

13. In civil proceedings, an adverse inference may be drawn from the invocation of the Fifth Amendment privilege not to testify. Baxter v. Palmigiano, 425 U.S. 308, 318 (1975); see also Lefkowitz v. Cunningham, 431 U.S. 801, 808, n.5 (1977). "While this refusal [to answer questions] may not be used as the sole basis of a prima facie case, it may nonetheless be used in conjunction with other evidence to establish a prima facie case." Director, OTS v. Lopez, 960 F.2d 958, 965 (11th Cir. 1992).

Directors had the power to appoint and remove the Trustee[14] and the Administrative Committee that was responsible for administering the ESOP and directing the Trustee. The Trustee had no independent authority, but rather was directed to invest the assets of the ESOP and to make distributions in the manner specified by the Administrative Committee. The Administrative Committee possessed all of the authority to make decisions with respect to the management of the ESOP and the disposition of its assets. The ACC Board of Directors' power to appoint the Administrative Committee members and Keating's participation in the ESOP's purchases of ACC shares of stock meant that all of the decisions with respect to the ESOP were controlled by ACC and Keating, as Chairman of the ACC Board of Directors. The Administrative Committee merely "rubber stamped" these decisions.

Motivated in part by his desire to sell his shares of ACC stock to the ESOP,[15] in the late spring through the summer of 1985, Keating directed ACC representatives to negotiate with Bankers Trust Company ("Bankers Trust") to raise money for the ESOP.[16] On

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14. On November 14, 1985, the Board of Directors of ACC appointed the First National Bank of Minneapolis to succeed the Northern Trust Company of Arizona as the Trustee of the ESOP.

15. Findings at ¶ 102-103; H.Ex. II-8 at 3.

16. Leveraging an ESOP is advantageous in that the ESOP may borrow funds to invest in a large block of the employer's stock more quickly than an ESOP could if it had to depend solely on the company's annual contributions to the ESOP for the necessary funds to purchase stock. FHLBB Op. by Williams, at 3, n.6 (January 31, 1986). In addition, an ESOP is able to obtain favorable interest rates on loans to purchase "employer securities" because 50 percent of interest on such loans is exempt from federal income taxes if paid to banks, insurance companies and other qualified entities. H.Ex. II-10; Findings ¶ 104.

November 21, 1985, the ESOP borrowed $20 million from institutional investors through the issuance of three series of floating rate ESOP notes ("FRESOP notes").[17] The first series of notes, the Series A notes, was backed by a Bankers Trust letter of credit secured by a $5 million pledge of assets and guarantee from ACC. The remaining notes, the Series B and C notes, were backed by Bankers Trust letters of credit secured by a $15 million pledge of assets and guarantee from Lincoln. The proceeds of the A Series notes were to be used to purchase shares of ACC from insiders; the proceeds of the B and C Series notes were to be used to purchase ACC shares from other sources.

The FRESOP notes could not have been issued without Lincoln's participation. Bankers Trust required that the amount of a FRESOP note offering be at least $20 million to ensure an adequate market for the notes. ACC did not have sufficient acceptable collateral to pledge for a $20 million offering. Therefore, the transaction could not be consummated without Lincoln's pledge and guarantee. Lincoln's pledge and guarantee on the B and C series were

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17. At that time, Bankers Trust had just begun marketing FRESOP notes that could be tendered, or "put" back, to Bankers Trust by the investor every 30 days. In order to facilitate this "put" feature, Bankers Trust required that the notes be secured by letters of credit, which in turn had to be fully collateralized by a pledge of assets. In the event investors exercised the "put" option and Bankers Trust could not remarket the notes immediately, the letters of credit would be drawn upon by Bankers Trust and the proceeds used to repurchase the FRESOP notes for Lincoln and ACC.

prohibited by applicable Federal Savings and Loan Insurance Corporation ("FSLIC") affiliated persons regulations and transactions with affiliates laws and regulations regardless of whose shares were purchased with the proceeds of the loan.

The Lincoln Board of Directors approved the $15 million pledge of assets on November 12, 1985. The minutes of the meeting show that Wischer, Hubbard, Keating III, Niebling and Andrew F. Ligget attended the meeting and approved the transaction. At that time, Wischer, Hubbard and Keating III were also the three members of the ESOP Administrative Committee (the "Old Administrative Committee"). Thus, at the time the first steps were taken to initiate the FRESOP note transaction, each of the members of the Administrative Committee that was designated to perform all the fiduciary functions of the ESOP, including directing the Trustee, was an officer and/or director of Lincoln.

On November 15, 1985, the members of the Old Administrative Committee were replaced by Richard Bertsch, James Millican, and Margaret Wong (the "New Administrative Committee"), three acquaintances of Respondent. On the same day as they were appointed, the New Administrative Committee members executed a resolution prepared by ACC approving the FRESOP note transaction exactly as it had been negotiated and structured by ACC at the direction of Keating. They also authorized the Trustee to use the proceeds of the FRESOP notes to purchase shares of ACC stock. These actions were taken without meetings or discussions among the members of the New Administrative Committee and without any investigation or due diligence review of the proposal by the New Administrative Committee to determine whether it was advisable for the ESOP.

Respondent and others at ACC solicited and arranged all of the purchases of the ACC shares made by the ESOP with the proceeds from the FRESOP notes. The entire $5 million in proceeds from the A Series of FRESOP notes was used to purchase a total of 606,601 shares of ACC stock from directors of ACC and members of their families. Keating himself received $1.65 million for the sale of 200,000 shares of ACC stock to the ESOP. The New Administrative Committee did not have any contact with the insiders and did not negotiate the purchases of the insider shares on behalf of the ESOP. These insider purchases were solicited by Keating and others at ACC and executed by the Trustee at the direction of ACC without the approval or authorization of the New Administrative Committee.

The majority of the proceeds from the B and C Series of notes were used to purchase a total of 1,400,000 shares of ACC stock from Drexel Burnham Lambert ("DBL") for $11,800,000. ACC arranged the trades for 1,000,000 of these shares and these trades were executed by ACC on November 14, 1985, prior to the appointment of the New Administrative Committee. The New Administrative Committee never authorized these initial purchases from DBL.

The remainder of the proceeds from the B and C Series of notes ($3.2 million) was used to purchase shares of ACC stock from third parties through private purchases as well as open market transactions. After the purchases were negotiated and confirmed by Keating and others at ACC, ACC prepared resolutions for the New Administrative Committee to execute approving the transactions. The New Administrative Committee never failed to execute a resolution prepared by ACC. After the FRESOP note transaction was completed, Keating continued to exercise control over the fiduciary decisions of the ESOP by directing the timing and distribution of shares to the ESOP plan participants.

On April 19, 1989, Bankers Trust declared the FRESOP notes to be in default as a consequence of the bankruptcy of ACC and the conservatorship of Lincoln. Bankers Trust drew upon the letters of credit to repay the FRESOP note investors, and then liquidated the collateral pledged by Lincoln. Bankers Trust used $11.2 million of the proceeds to satisfy Lincoln's obligation under the guarantee of the letters of credit that supported the B and C Series of notes. In addition to losing $11.2 million of the collateral pledged to secure the letters of credit, Lincoln recognized a loss in the amount of $1,012,738.76, which represented the difference between the value of the liquidated collateral on Lincoln's books and the sales price, or market value, of the collateral at the time of its liquidation. Lincoln's loss as a result of the pledge of assets to secure the FRESOP notes was $12.2 million.

Keating directed ACC officers and directors to seek ESOP financing from Bankers Trust and to negotiate the terms of such financing. Keating was kept apprised of the meetings with Bankers Trust. As a member of the Board of Directors of ACC, he approved the FRESOP transaction on behalf of ACC. In addition, Keating personally selected the members of the New Administrative Committee of the ESOP; made the fiduciary decisions with respect to the ESOP that should have been made by the Administrative Committee; and arranged for the ESOP to purchase shares of ACC stock from Keating and members of his family, other ACC insiders and third parties. As a controlling shareholder of Lincoln, and in actual fact, Keating had the power over decision making at Lincoln. Keating asserted his Fifth Amendment privilege against self-incrimination at the April/May 1992 phase of the hearing when asked if he directed Lincoln to pledge $15 million in assets and to guarantee the letters of credit from Bankers Trust and if he directed and controlled the Administrative Committee.

C. ALJ's Recommended Decision

At the times relevant for purposes of this proceeding, the FSLIC insurance regulations placed *per se* prohibitions on certain transactions that might result in self-dealing and the associated risks to the safe and sound operation of savings associations and to the Federal deposit insurance funds. *See* 12 C.F.R. § 563.43 (1985). In addition, former section 408(d) of the National Housing Act ("NHA"), and the regulations promulgated thereunder relating to holding companies of insured institutions, placed further restrictions upon self-dealing between holding companies and the subsidiaries they control. See 12 U.S.C. § 1730a(d) (1988)[18] and 12 C.F.R. § 584.3 (1985).

The FSLIC insurance regulations prohibited savings associations, except under certain narrowly defined circumstances, from making or guaranteeing any loan or extension of credit to "affiliated persons," such as directors, officers and others who might be in a position to exercise control over the operation of the institution. See 12 C.F.R. §§ 561.29 (definition of "affiliated person")[19] and 563.43(b), (c)(5) (1985) (prohibitions on certain transactions with affiliated persons). The rules relating to savings and loan holding companies prohibited these same transactions between an insured institution and any "affiliate," that is, any person or entity that controls, is controlled by or is under common control with such institution. See 12 C.F.R. § 583.15 (1985) (definition of "affiliate"); and 12 U.S.C. § 1730a(d)(4) and

18. Sections 407 and 408 of the NHA -- both repealed by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 -- were formerly codified at 12 U.S.C. §§ 1730 and 1730a., respectively. Citations are to § 1730 and § 1730a as they appeared in the 1988 edition of the United States Code. Current statutory provisions, comparable in substance to former NHA sections 407 and 408, are set forth at 12 U.S.C. §§ 1463(a), 1464(d), 1467a (regulation of savings associations and their holding companies) and 1818 (enforcement authority).

19. The definition of "affiliated person" incorporates the concept of a "controlling person" of a thrift, defined in 12 C.F.R. § 561.28 (1985).

(5) (1988) and 12 C.F.R. § 584.3(a)(4) and (5) (1985) (prohibitions on certain transactions with affiliates).

The ALJ determined that the advance and extension of credit to HPLP from Lincoln subsidiaries: were impermissible conflicts of interest and self-dealing that violated the prohibition on transactions with affiliated persons, 12 C.F.R. § 563.43(b) (1985); were unsafe and unsound practices because they were contrary to prudent lending practices and placed Lincoln at an abnormal risk of loss; were breaches of Keating's fiduciary duties of loyalty and care to Lincoln because his personal interest in receiving tax benefits was in conflict with the interests of Lincoln in making prudent loans, in violation of 12 C.F.R. § 571.7 (1985); were undertaken with reckless disregard of applicable laws and regulations and with willful and continuing disregard for the safety and soundness of Lincoln; and enriched Respondent unjustly. The ALJ found that Keating personally, and in combination with others, caused, brought about and participated in the advance and extension of credit to HPLP, which resulted in losses to Lincoln of over $24.2 million.

The ALJ further determined that Lincoln's pledge of assets and guarantee of the obligations of the ESOP: were unsafe and unsound practices that violated conflict of interest standards, including those contained in 12 C.F.R. § 571.7 (1985); violated transactions with affiliates and affiliated persons laws and regulations, including 12 C.F.R. §§ 563.43(b)(1) and (c)(5), 584.3(a)(4) and (5) (1985); were breaches of Respondent's fiduciary duty as controlling shareholder of Lincoln because his personal financial interest in selling his ACC stock conflicted with Lincoln's financial interests; were undertaken with reckless disregard of applicable laws and regulations and with willful and continuing disregard for the safety and soundness of Lincoln; and enriched Respondent unjustly. The ALJ found that Keating directed the negotiation of the FRESOP note transaction and that he personally, and in combination with others, made the fiduciary decisions with respect to the ESOP. Finally, Lincoln suffered losses of over $12.2 million as a result of the ESOP transaction.

Accordingly, the ALJ recommended a cease and desist order directing restitution to Lincoln for the losses sustained by the institution, against Keating. Additionally, the ALJ recommended that Keating be prohibited from future participation in the conduct of the affairs of any insured institution.

The ALJ's recommended decision, including his findings of fact and conclusions of law, parallel the only substantive filings received, those of Enforcement Counsel. Despite repeated opportunities, Respondent has failed to make any substantive presentations or filings setting forth his perspective of the facts or applicable law in the proceeding. Respondent neither testified nor put on evidence at the hearing, though his counsel cross-examined Enforcement Counsel's witnesses during the July 1991 phase of the hearing. He did not file proposed findings of fact or conclusions of law. His exceptions contained no specific challenge to the ALJ's Recommended Decision and merely repeated arguments made in earlier filings in this proceeding, all of which have been rejected.

The ALJ's Recommended Decision is supported by the record. The ALJ has made the requisite findings of fact and drawn the appropriate conclusions of law warranting the imposition of the remedies sought by Enforcement Counsel. Therefore, the Acting Director affirms the ALJ's Recommended Decision, except insofar as it is inconsistent with this Final Decision and Order and adopts the ALJ's findings of fact and conclusions of law concerning Keating's liability. The bases for the Acting Director's decision are summarized in the Discussion below.

III. DISCUSSION

A. Statutory Authority

1. Jurisdiction and Authority to Impose Remedies

Under the Federal Deposit Insurance Act ("FDIA"), as amended by the Financial Institution Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"), OTS is the appropriate federal banking agency to initiate administrative proceedings against officers, directors and other institution-affiliated parties[20] of federally-insured

20. Under § 204 of FIRREA, 12 U.S.C. § 1813(u) (Supp. IV 1992), an institution-affiliated party includes, inter alia, a director, officer, employee, or controlling stockholder, or other person who participates in the conduct of the institution's affairs.

savings and loan associations, including state savings associations such as Lincoln. Such administrative proceedings may take the form of cease-and-desist proceedings under section 8(b) of the FDIA, 12 U.S.C. § 1818(b) (Supp. IV 1992), and former section 407(e) of the NHA, 12 U.S.C. § 1730(e) (1988); and removal and prohibition actions under section 8(e) of the FDIA, 12 U.S.C. § 1818(e) (Supp. IV 1992), and former section 407(g) of the NHA, 12 U.S.C. § 1730(g) (1988).

In his exceptions to the Recommended Decision, Respondent challenges the OTS's jurisdiction to institute this proceeding against him. The Director has already determined that OTS has jurisdiction to bring this action and that the agency has the authority to impose the remedies sought in the Amended Notice. OTS Order No. AP 91-20 (May 11, 1991) ("Jurisdiction Order");[21] see

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21. In the Jurisdiction Order, the Director also rejected Respondent's argument, repeated in his exceptions, that Director Ryan should have been recused from this proceeding.

In addition, in his exceptions, Respondent asserts that the creation of the OTS was an unconstitutional act of Congress and the hearing was conducted in violation of his constitutional and civil rights, including his right to trial by jury under the Seventh Amendment to the Constitution. There is no merit to Keating's claim that he is entitled to a jury trial under the Seventh Amendment to the Constitution. Courts have rejected similar claims against the OTS where, as here, "there is a proper administrative forum for adjudicating public rights." Akin v. OTS, 950 F.2d 1180, 1186 (5th Cir. 1992). In addition, notwithstanding the lack of specificity of Respondent's other arguments, the Director has reviewed similar constitutional claims made by Respondent in earlier filings and has found that they were appropriately rejected. See Jurisdiction Order. See also ALJ Order dated November 15, 1990 (denying Keating Respondents' Motion to Stay).

Keating v. OTS, 779 F. Supp. 1053 (D. Ariz. 1991). See also ALJ's Recommended Decision at 7-8. The conduct at issue in this proceeding occurred between November, 1984, and April, 1989. As set forth in detail in the Jurisdiction Order, the post-FIRREA remedies set forth in section 8(b) and (e) of the FDIA, 12 U.S.C. § 1818(b) and (e) -- cease and desist orders requiring restitution and industry-wide prohibition orders -- may be applied to Respondent's conduct. The substantive standards for judging that conduct, however, are those found in the law in effect during the time of the conduct complained of, that is, former sections 407(e) and (g) of the NHA, 12 U.S.C. § 1730(e) and (g) (1988). See Jurisdiction Order at 17-23.

Respondent was the Chairman of the Board and the largest shareholder[22] of ACC at all relevant times, and he was President and Chief Executive Officer of ACC from September 1981 through May 1985. ACC owned 100 percent of the stock of Lincoln. Therefore, Respondent was a "controlling person"[23] of Lincoln. The ALJ determined that Respondent dominated, controlled and supervised

22. At all relevant times, Keating was the largest shareholder of ACC. H.Ex. II-1 ¶ 13(a). ACC's 1986 proxy statement lists Respondent as the owner of 24.2 percent of the company's common stock. Id. ACC's 1987 proxy statement reveals that Respondent owned 21 percent of the company's common shares in 1987. H.Ex. II-40 at 1.

23. A "controlling person" includes any person who directly or indirectly owns or controls ten percent or more of the voting shares or rights of such institution. 12 C.F.R. § 561.28 (1985).

Lincoln and its subsidiaries. In particular, the ALJ found that Respondent took an "extreme" interest in Lincoln; that the Lincoln Board of Directors reported directly to Respondent; that Respondent originated an inordinate amount of business for Lincoln himself; and that he was very involved in and exercised control over many of the operations of Lincoln and its subsidiaries. Therefore, Respondent was clearly a "person participating in the conduct of the affairs"[24] of Lincoln, both directly and through his relationship with ACC; and was an institution-affiliated party with respect to Lincoln.

2. Cease and Desist Order

The OTS may issue a cease and desist order against any person participating in the conduct of the affairs of an insured institution who, inter alia, engaged in an unsafe or unsound practice in conducting the business of an institution or who violated[25] a law, rule or regulation.[26] The agency may also "take affirmative action to correct the conditions resulting from any

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24. See In the Matter of Seals, OTS Order No. AP 92-115 (October 21, 1992) (appeal pending).

25. The term "violates" includes "any action (alone or with others) for or towards causing, bringing about, participating in, counseling, or aiding or abetting a violation." 12 U.S.C. § 1730(k)(3)(A) (1988); 12 U.S.C. § 1813(v) (Supp. IV 1992).

26. For post-FIRREA conduct, essentially the same standards apply. 12 U.S.C. § 1818(b) authorizes a cease and desist order if an institution-affiliated party has engaged in proscribed activities, including: engaging in an unsafe an unsound practice in conducting the business of the association; or violating a law, rule or regulation.

such violation or practice." Former section 407(e)(1) of the NHA, 12 U.S.C. § 1730(e)(1) (1988); see also 12 U.S.C. § 1818(b).

If the pre-FIRREA conduct supports a cease and desist order, then the OTS may order an institution-affiliated party to make restitution or provide reimbursement if a violation or an unsafe or unsound practice resulted in a party being "unjustly enriched" or involved "reckless disregard" for the law or any applicable regulation. 12 U.S.C. § 1818(b)(6)(A). See also Akin v. OTS, 950 F.2d 1180, 1183-84 (5th Cir. 1992).

3. Removal and Prohibition Order

The OTS may order a person to be removed from office and prohibited from participating in the conduct of the affairs of that insured institution if the OTS determines, with respect to any person participating in the conduct of the affairs of an insured institution, that:

> (1) by reason of such person's conduct or practice with respect to such institution or other business entity, the insured institution has suffered substantial financial loss or other damage;
>
> (2) such conduct or practice evidences personal dishonesty or a willful or continuing disregard for the safety and soundness of the insured institution; and
>
> (3) such conduct or practice evidences such person's unfitness to participate in the conduct of affairs of such institution.

Former section 407(g)(2) of the NHA, 12 U.S.C. § 1730(g)(2) (1988); see also 12 U.S.C. § 1818(e).[27] If the pre-FIRREA conduct supports a removal and prohibition order with respect to a particular institution under former section 407(g) of the NHA, then the industry-wide ban provided for in 12 U.S.C. § 1818(e)(7) is also available. See Jurisdiction Order at 19-20.

B. Violations of Laws and Regulations

1. The HPLP Transaction Violated the Prohibition on Affiliated Persons Transactions

At the time the HPLP transaction was undertaken, the regulations applicable to Lincoln prohibited certain transactions between insured institutions and their "affiliated persons." The purpose of these prohibitions was to prevent insured institutions from directly or indirectly entering into "transactions with third parties from which affiliated persons would derive benefit, or which could place the institution or subsidiary in a position of having to choose between acting in the best interests of itself or the affiliated person." 41 Fed. Reg. 35812, 35819 (August 24, 1976). The HPLP transaction was subject to the regulations because HPLP was an "affiliated person" of Lincoln.

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27. For post-FIRREA conduct, 12 U.S.C. § 1818(e) authorizes a removal and prohibition order where an institution-affiliated party violated any law or regulation, engaged or participated in an unsafe or unsound practice or breached his fiduciary duty; by reason of such violation, practice or breach, the insured depository institution suffered loss or the party received gain; and such violation, practice or breach involves personal dishonesty or demonstrates willful or continuing disregard for the safety or soundness of the institution.

Under the conflict rules in effect at the time of the transactions at issue, the term "affiliated person" of an insured institution included a director, officer or controlling person of the insured institution, a spouse of such person, or an immediate family member of such person who is a director or an officer of any subsidiary of the insured institution. 12 C.F.R. § 561.29(a)-(c).

Keating was a "controlling person" of Lincoln within the meaning of 12 C.F.R. § 561.28 (1985). Respondent owned more than 10 percent of the stock of ACC, and therefore controlled more than 10 percent of the voting shares of Lincoln, a wholly owned subsidiary of ACC. In addition, as discussed in detail in section II.B.1., in actual fact Keating dominated, controlled and supervised Lincoln and its subsidiaries. Several members of Keating's immediate family were officers or directors of Lincoln or its subsidiaries and, therefore, Keating, and several members of his immediate family, were affiliated persons of Lincoln.

An organization is an "affiliated person" of an insured institution if a director, officer or controlling person of an insured institution:

> [i]s a limited partner [of the organization] who, directly or indirectly either alone or with his spouse and the members of his immediate family who are also affiliated persons of the institution, owns an interest of 10 percent or more in the partnership (based on the value of the contribution) or who, directly or indirectly with other directors, officers and controlling persons of such institution and their spouses and their immediate family members who are also

> affiliated persons of the institution, owns an interest of 25 percent or more in the partnership.

12 C.F.R. § 561.29(d)(3) (1985).

Respondent and members of his immediate family who were affiliated persons of Lincoln, owned or controlled more than 10 percent of HPLP. H.Ex. I-114 at 64-68. At the same time, Respondent, members of his immediate family who were affiliated persons of Lincoln, and officers and directors of Lincoln and their immediate families owned more than 35 percent of HPLP.[28] Id. at 69-70. Furthermore, the record demonstrates that in fact Respondent controlled all aspects of HPLP's and the Hotel's financings and operations, including: directing the purchase and renovation of the Hotel; attending weekly meetings at which decisions on operations were made; hiring and firing the Hotel management; and approving the budget for the Hotel. Therefore, HPLP was an "affiliated person" of Lincoln.

The applicable rules prohibited an insured institution or any of its subsidiaries from either directly or indirectly making a loan to any affiliated person of the institution, except under certain defined circumstances not applicable here. 12 C.F.R. § 563.43(b) (1985). This prohibition was breached twice in the HPLP transaction. CHG/M, a subsidiary of Lincoln, made a $10.4 million

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28. Ownership interest by affiliated persons of an insured institution in an entity is a critical element in determining whether such entity is an affiliated person of an insured institution. See FHLBB Op. by McGraw, January 25, 1978.

advance to HPLP, an affiliated person of Lincoln, to cover HPLP's operating losses. PFC, a subsidiary of Lincoln, made an extension of credit of $20 million to HPLP, used in part by HPLP to pay off the $10.4 million advance it received from CHG/M. Therefore, the advance and the extension of credit violated regulations prohibiting transactions with affiliated persons.[29]

Keating was a controlling shareholder of Lincoln and in fact controlled the operations of Lincoln and its subsidiaries, even though he was not an officer or director of those entities. The evidence of Keating's domination in general of Lincoln and its subsidiaries and of his control of HPLP's and the Hotel's financing and operations is overwhelming. In accordance with established legal precedent as well, an adverse inference may be drawn from Keating's refusal to testify concerning whether he directed the advance and extension of credit, providing further evidence that Keating violated regulations and engaged in unsafe and unsound practices.[30] Thus, the Acting Director concludes that Keating

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29. In addition, the purchase of the Hotel Pontchartrain by HPLP was accounted for on the books of CHG/M as a "sale" even though CHG/M was the general partner of HPLP. Such accounting treatment violated FAS 66 and led to inflated financial statements of CHG/M and, therefore, indirectly, Lincoln. This was a violation of 12 C.F.R. § 526.23-3 (1985), which required that the financial statements of an institution fairly reflect its financial condition.

30. See n.13, supra.

In an order issued simultaneously with this Decision and Order, the Acting Director denies a late-filed request by Respondent that the proceeding be re-opened so that he might testify. Respondent earlier had appeared as a witness but had invoked his Fifth Amendment privilege not to testify. To the extent Respondent's argument is that it is inappropriate for the Acting Director to draw adverse inferences from Respondent's participated in violations of regulations prohibiting transactions with affiliated persons.

2. ESOP Transaction

a. Prohibited Affiliated Persons Transaction

An "affiliated person" of an insured institution includes:

> [a]ny trust or other estate in which a director, officer, or controlling person of such [insured] institution or the spouse of such person has a substantial beneficial interest or as to which such person or his spouse serves as a trustee or in a similar fiduciary capacity.

12 C.F.R. § 561.29(e)(1985).

In this case, the ESOP constituted an affiliated person of Lincoln because directors, officers and controlling persons of Lincoln also served the ESOP in a fiduciary capacity similar to a trustee. Under the terms of the ESOP plan, the duties of the Administrative Committee included: directing the investment of trust assets by the Trustee, determining the price at which the trust would acquire shares of ACC stock, and directing the sale or resale of ACC shares; determining the timing and method of

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(Footnote 30 continued from previous page)
refusal to testify, the Acting Director concludes in the alternative that, leaving aside Respondent's refusal to testify and his invocation of the Fifth Amendment, the facts adduced at the hearing are sufficient to prove the violations and unsafe and unsound practices alleged and to support the remedies ordered herein.

distribution of shares to participants and beneficiaries; and voting the shares of ACC stock held by the trust that were not allocated to participant accounts. By virtue of these responsibilities, the Administrative Committee was acting in a "similar fiduciary capacity" to a trustee.[31]

At all relevant times, the Administrative Committee was either composed of or under the control of officers and directors of ACC and Lincoln, including Keating. The Old Administrative Committee was composed exclusively of officers and directors of Lincoln. Respondent, a controlling person of Lincoln, and other officers and directors of ACC[32] selected the New Administrative Committee, which was composed of acquaintances of Respondent. Respondent and others at ACC dictated the operations and decision making of the New Administrative Committee. Rather than exercising independent fiduciary discretion with respect to the ESOP, the New Administrative Committee simply served as a "rubber stamp" and approved whatever resolutions ACC prepared regarding every aspect of the ESOP's operation in general, and its participation in the

31. The FHLBB determined that a "similar fiduciary capacity" includes

> any position which involves the power to vote unallocated shares held in the ESOP, the power to acquire or dispose of the assets of the trust, or the power to determine when and how employees may receive distribution from the trust. . . .

FHLBB Op. by Williams (January 13, 1987).

32. ACC owned 100 percent of the stock of Lincoln and therefore was also a controlling person of Lincoln. See 12 C.F.R. § 561.28 (1985).

FRESOP note transaction in particular. Through this control of the Old Administrative Committee and the New Administrative Committee, directors, officers and controlling persons of Lincoln were acting in a "similar fiduciary capacity" to a trustee. Therefore, the ESOP was an affiliated person of Lincoln.

An insured institution and its subsidiaries are prohibited from entering into any guarantee arrangement with respect to a loan made by any third party to any affiliated person of such institution. 12 C.F.R. § 563.43(c)(5) (1985). Lincoln pledged collateral and issued a guarantee to secure the ESOP's, an affiliated person's, debt to Bankers Trust. This pledge and guarantee violated the affiliated persons regulations.[33]

b. <u>Prohibited Transactions With Affiliates</u>

In addition to the prohibitions in the applicable regulations on transactions with affiliated persons, former section 408 of the NHA, 12 U.S.C. § 1730a (1988), and the regulations promulgated thereunder relating to holding companies of insured institutions, placed further restrictions upon self-dealing between insured institutions and their "affiliates."

33. The pledged collateral was to be used to purchase the FRESOP notes if investors "put" the FRESOP notes back to Bankers Trust and the notes could not be remarketed. Therefore, the pledge and guarantee were also an extension of credit to the ESOP, in violation of 12 C.F.R. § 563.43(b) (1985).

An "affiliate" of an insured institution means any person or company that controls, is controlled by, or is under common control with, such insured institution. 12 C.F.R. § 583.15 (1985). "Control" is defined to include the ability to directly or indirectly exercise a controlling influence over the management or policies of such institution, as well as control over the appointment of a majority of the trustees of a trust. 12 C.F.R. § 583.26(b) and (d) (1985).[34]

As described above in Part II.B.1., Lincoln was controlled by ACC and Keating: Keating was a controlling shareholder of Lincoln and he in fact dominated Lincoln's operations. The ESOP was also controlled by ACC and Keating: ACC selected the Administrative Committee of the ESOP and controlled its decision making; every aspect of the ESOP's operations were controlled by persons selected by ACC; and ACC controlled the appointment of the ESOP's Trustee. Therefore, the ESOP was an "affiliate" of Lincoln because the ESOP and Lincoln were under the common control of ACC, its Board of Directors and Respondent.

An insured institution is prohibited from guaranteeing the repayment of any loan or extension of credit granted to any

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34. "If an insured institution or the holding company directly or indirectly controls the selection of the ESOP Trustee, the ESOP generally would be deemed an 'affiliate' of the institution." FHLBB Op. by Williams at 2-3 (July 18, 1988). <u>See also</u> FHLBB Op. by Williams at 3 (April 14, 1989).

affiliate by any third party. 12 C.F.R. § 583.4(a)(5) (1985).[35] Therefore, Lincoln's guarantee of the ESOP's debt to Banker's Trust violated transactions with affiliates regulations.

As to Keating's participation in the ESOP transaction, Keating was a controlling shareholder of Lincoln and in fact dominated decision making at Lincoln. The evidence is uncontroverted that Keating controlled the decisionmaking by the ESOP and that he initiated and monitored the ESOP transaction. Furthermore, an adverse inference may be drawn from Keating's refusal to testify concerning whether he directed Lincoln's approval of the pledge of assets and guarantee for the ESOP's debt, providing further evidence that Keating violated transactions with affiliates law and regulations (as well as engaging in unsafe and unsound practices).[36] Thus, the Acting Director concludes that Keating participated in violations of the laws and regulations that prohibit transactions both with affiliates and with affiliated persons.

C. Unsafe And Unsound Practices

An unsafe and unsound practice involves conduct

> that is contrary to generally accepted standards of prudent operation of a financial institution, the possible consequence of which, if continued, may be

35. The transactions also violated the provisions prohibiting loans to affiliates. See 12 C.F.R. § 583.4(a)(4) (1985).

36. As to this inference, see n.30, supra.

abnormal risk, or loss or damage to an institution, its shareholders, or the Federal deposit insurance funds.

In the Matter of Simpson, OTS Order No. 92-123, 15, n.16 (November 18, 1992) (appeal pending). See Saratoga Savings & Loan Ass'n v. FHLBB, 879 F.2d 689, 693 (9th Cir. 1989); First Nat'l Bank of Eden v. Dept. of the Treasury, 568 F.2d 610, 611, n.2 (8th Cir. 1978).[37]

Because of the risk that affiliated persons who control thrift institutions may use their positions for their personal benefit to the detriment of the thrift, self-dealing and impermissible conflicts of interest are regarded as inherently unsafe and unsound practices. Hoffman v. FDIC, 912 F.2d 1172, 1174 (9th Cir. 1990); Independent Bankers Ass'n of America v. Heimann, 613 F.2d 1164, 1168-69 (D.C. Cir.), cert. denied, 449 U.S. 823 (1980). See also 12 C.F.R. § 571.7(b) (1985). It is an unsafe and unsound practice for officers, directors and other affiliated persons, including controlling persons, of insured institutions to place themselves in a position where their personal financial interests are in conflict with the interests of the insured institution. See Id.

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37. The ALJ erroneously used the standard for "unsafe and unsound" conduct set forth in Gulf Federal Savings & Loan Ass'n v. FHLBB, 651 F.2d 259, 264 (5th Cir. 1981), cert. denied, 458 U.S. 1121 (1982), that additionally requires a reasonably direct effect on the institution's financial soundness. The OTS has previously determined that the standard set forth in the Saratoga and Eden cases is the appropriate standard to apply. See In the Matter of Bush, Final Decision and Order, OTS Order No. AP 91-16, 30-31 (April 18, 1991); In the Matter of Seidman, Decision and Order, OTS Order No. AP 92-149 (December 4, 1992) (appeal pending). In this case, there clearly was financial harm to the institution from Respondent's conduct. Thus, the ALJ's error does not affect the validity of his conclusions.

1. HPLP Transaction

Respondent engaged in unsafe and unsound practices with respect to the HPLP transaction. Respondent, as a limited partner in HPLP, had a personal financial interest in its continued viability. The value of HPLP to Respondent was Respondent's ability, for income tax purposes, to offset gains from other enterprises with the losses from his interest in HPLP. If the Hotel defaulted on its mortgage and was put into foreclosure, Respondent would lose the value of these tax savings. Therefore, Respondent had an interest in ensuring that HPLP received financing to cover its operating losses. Respondent's personal financial interests were in conflict with Lincoln's interest in making prudent loans and conducting its underwriting in accordance with standards of safety and soundness.

Respondent, through his control of Lincoln and its subsidiaries, allowed Lincoln's subsidiaries to make an advance and an extension of credit to HPLP that were contrary to prudent lending practices: they were on preferential terms (Recommended Decision at 40), the loans were made to cover operating losses, there was no underwriting, and there was no board of directors approval for the loans. Findings ¶¶ 45-48.

2. ESOP Transaction

Respondent also engaged in unsafe and unsound practices with respect to the ESOP transaction. Keating, through his control over the management and policies of Lincoln, directed Lincoln's approval of the pledge of assets and guarantee on behalf of the ESOP. Keating had a personal financial stake in selling his shares of stock to the ESOP. This interest was in conflict with the interest of Lincoln in complying with law and regulations prohibiting transactions with affiliates and affiliated persons.

In addition, Keating directed ACC employees to obtain financing for the ESOP and was kept apprised of the status of meetings with Bankers Trust. Findings at ¶¶ 101-102, 115. The structure of the transaction that was negotiated made any pledge of assets and guarantee by Lincoln an unsafe and unsound practice. The FRESOP notes were subject to a cross-default provision, that is, a default by ACC (an entity beyond Lincoln's control) on its obligations on the A series notes would trigger Lincoln's obligations on its guarantee and pledge of assets on the B and C series notes. Findings ¶ 217.

Therefore, the Acting Director concludes that Respondent engaged in unsafe and unsound practices with respect to the HPLP and the ESOP transactions.

D. Breaches of Fiduciary Duty

Directors and officers owe a fiduciary duty of loyalty to the institutions they serve. This duty requires directors and officers to administer the affairs of the institution with candor, personal honesty and integrity. In the Matter of Simpson, at 20. They are prohibited from advancing their own personal or business interests, or those of others, at the expense of the institution. In the Matter of Bush, at 13, 14; Pepper v. Litton, 308 U.S. 295, 306 (1939). The standards elucidating an officer's or director's fiduciary duty appeared, at the times relevant to this proceeding, at section 571.7 of the agency's rules. It provides that directors and officers have a fundamental obligation "to avoid placing [themselves] in a position which creates, or which leads to or could lead to, a conflict of interest or appearance of a conflict of interest." 12 C.F.R. § 571.7(b) (1985). See also In the Matter of Simpson, at 20; In the Matter of Bush, at 10-11.

In addition to the fiduciary duty of loyalty, directors and officers owe a fiduciary duty of care to the institution. The Supreme Court has defined that duty as

> that [degree of care] which ordinarily prudent and diligent men would exercise under similar circumstances, and in determining that, the restrictions of the statute and the usage of business should be taken into account.

Briggs v. Spaulding, 141 U.S. 132 (1891). This duty requires directors and officers to act diligently, prudently, honestly and carefully to ensure their institution's compliance with state and federal banking laws and regulations. In the Matter of Simpson, at 21-22; In the Matter of M, FHLBB Res. 89-537, at 41-42 (March 5, 1989).

Those who effectively control the operations of a financial institution through stock ownership or through _de facto_ control owe fiduciary duties similar to those of a director. _See Pepper v. Litton_, 308 U.S. at 306-07; _Banco De Desarrollo Agropecuario v. Gibbs_, 709 F. Supp. 1302, 1306-07 (S.D.N.Y. 1989); J. Villa, _Bank Directors' Officers' and Lawyers' Civil Liabilities_ § 1.02[C] (1992). A dominant or controlling shareholder's powers are in trust, like a director's and, therefore, his or her dealings with the corporation are subject to the same "rigorous scrutiny." _Pepper v. Litton_, 308 U.S. at 306-07.

With respect to the HPLP transaction, Keating breached his fiduciary duties by his active manipulation of Lincoln for his own benefit. Keating, as the controlling shareholder of Lincoln, breached his fiduciary duty of loyalty to the association by permitting Lincoln subsidiaries to make the advance and extension of credit that led to personal financial benefits for himself and other insiders in the form of tax credits and that at the same time, exposed Lincoln and its subsidiaries to additional risks. The duty of loyalty precludes an insider from engaging in transactions, such as the advance and extension of credit to HPLP, that create an impermissible conflict between the insider's personal financial interests and the financial interests of the institution itself.

Respondent breached his fiduciary duty of care by failing to ensure: proper underwriting of the line of credit; appropriate financial analysis before permitting the advance and extension of credit; and adequate internal controls and procedures for the proper approval of the advance and extension of credit.

With respect to the ESOP transaction, members of Lincoln's Board of Directors owed Lincoln a fiduciary duty of loyalty not to engage in any transaction on behalf of the institution where their personal financial interests were in actual or potential conflict with the financial interests of Lincoln. Keating, as a controlling shareholder of Lincoln who in fact controlled the operations of Lincoln, owed the institution the same fiduciary duty as its directors. Lincoln's Board of Directors and Keating breached this duty by approving Lincoln's pledge of assets and guarantee of the ESOP's B and C series of notes (which are *per se* prohibited under affiliated persons and transactions with affiliates laws and regulations), since part of the proceeds of the FRESOP note transaction were used to purchase shares of stock from Keating and other Lincoln insiders. At the same time that Keating profited from Lincoln's pledge, Lincoln itself was exposed to serious and additional risks.

E. Grounds Exist for the Entry of a Cease and Desist Order Directing Restitution Against Respondent

Keating's participation in violations of affiliated persons and transactions with affiliates law and regulations, and unsafe and unsound practices, including breaches of his fiduciary duties of loyalty and care, provide an appropriate basis for imposing a cease-and-desist order pursuant to 12 U.S.C. § 1818(b)(1).

In addition, Respondent was "unjustly enriched" by these violations and practices, which also "involved a reckless disregard for the law or any applicable regulations" within the meaning of 12 U.S.C. § 1818(b)(6)(A). Accordingly, the Acting Director will order Keating to take affirmative action to correct the conditions resulting from the violations and practices by making restitution to Lincoln of the losses it suffered by reason of the HPLP and ESOP transactions.

1. Respondent Was Unjustly Enriched by the HPLP and ESOP Transactions

Although the term "unjust enrichment" is not defined in the statute, recent case law has established that the term should be construed broadly and a respondent is unjustly enriched when he gains a "significant personal benefit" through unlawful means.[38] Respondent received significant personal benefits through his participation in the violations, unsafe and unsound practices and breaches of fiduciary duty at issue in this proceeding. As a limited partner of HPLP, Respondent received tax benefits from the Hotel's losses. Respondent's reported tax savings from 1985-1989 were over $700,000 by virtue of his 7.92 percent ownership interest

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38. Akin v. OTS, 950 F.2d 1180, 1184 (5th Cir. 1992) (respondent received significant personal benefit by retaining and disposing of funds that he was required to contribute to the association under a net worth maintenance agreement).

in HPLP. Respondent caused the ESOP to purchase 200,000 shares of ACC stock from him for $1.65 million with the proceeds of the FRESOP note sales. Therefore, Respondent was unjustly enriched by virtue of his participation in the HPLP and ESOP transactions.

2. Reckless Disregard For Law Or Regulation

For the purposes of section 8(b)(6)(A) of the FDIA, reckless disregard for the law, applicable regulations, or an agency order exists when: (1) the party acts with clear neglect for, or plain indifference to, the requirements of the law, applicable regulations or agency order of which the party was, or with reasonable diligence should have been, aware; and (2) the risk of loss or harm or other damage from the conduct is such that the party knows it, or it is so obvious that the party should have been aware of it. 12 U.S.C. § 1818(b)(6)(A); In the Matter of Simpson, at 17-19.

With respect to the HPLP transaction, the evidence shows that Respondent acted with plain indifference to and willfully ignored the requirements of the law when he brought about and participated in the advances and extension of credit to HPLP. Lincoln engaged in a convoluted scheme to finance the purchase of the Hotel by HPLP, such that there was no loan directly from Lincoln or its subsidiaries to HPLP,[39] in order to avoid the regulations

39. Rather than Lincoln making a loan directly to HPLP, one Lincoln subsidiary made a loan to another Lincoln subsidiary with HPLP then acquiring the Hotel. Findings ¶ 31.

restricting loans to affiliated persons. Findings ¶ 31; Transcript at 2598-2601 (Conner). Thus, ACC and Lincoln officers and directors knew from the inception of HPLP that any loans from Lincoln or any of its subsidiaries directly to HPLP would violate affiliated persons regulations. Id. In addition, just six weeks before the $20 million extension of credit was granted, ACC regulatory counsel alerted Respondent to a legal opinion Lincoln had secured from an outside law firm that concluded that Lincoln could not make a loan relating to the Hotel because HPLP was an affiliated person of Lincoln. Findings ¶ 65. In the face of the awareness of the restriction on loans to affiliated persons, the $10.4 million in advances and the $20 million extension of credit from Lincoln subsidiaries to HPLP clearly were made in reckless disregard of banking laws and regulations.

Likewise, in the case of the FRESOP notes, the evidence clearly shows that Respondent acted with plain indifference to and willfully ignored the regulations that prohibited Lincoln's pledge of assets to secure the ESOP notes, and intentionally allowed the violations to persist. At the outset of the transaction, officials at ACC, including Respondent, understood, based upon their experiences with an earlier loan to the ESOP, that applicable regulations restricted the manner in which Lincoln could make loans and extend credit to its affiliates and affiliated persons.[40] They

40. In the spring of 1985, Niebling, at the direction of Keating, arranged for the ESOP to borrow $3 million from Valley National Bank. The loan was secured by a pledge of collateral from ACC because ACC's regulatory counsel advised Niebling that under FHLBB regulations there was a prohibition against Lincoln guaranteeing the loan. Findings ¶¶ 95-100.

therefore prepared a false statement of facts concerning the independence of the Trustee to obtain a legal opinion concluding that Lincoln could participate in the transaction because the pledge and guarantee would not violate FSLIC regulations. Findings ¶¶ 172-81. Had the true facts been revealed, the law firm that issued the opinion would never have been able to render the opinion and the transaction could not have been consummated. Findings ¶¶ 172, 181.

Within three months of the consummation of the FRESOP note transaction, Respondent became aware, through a FHLBB opinion letter[41] and discussions with counsel, that Lincoln's pledge of collateral for the ESOP's obligation violated various applicable laws and regulations. Findings ¶¶ 182-86. Notwithstanding this knowledge, Respondent and other ACC insiders failed to take any steps to correct or undo Lincoln's pledge, or to substitute alternative collateral other than that of Lincoln to secure the ESOP financing. Findings ¶¶ 187-96. Instead, they willfully allowed Lincoln's prohibited pledge of $15 million in collateral to remain in place for over three years until the notes went into default in 1989. Id. Keating acted with willful and intentional indifference to the requirements of the law after learning that his actions were prohibited by applicable regulations. Thus, the

41. FHLBB Op. by Williams (January 31, 1986).

continued pledge of assets and guarantee by Lincoln clearly involved Keating's reckless disregard for the law and applicable regulations.

3. Lincoln's Losses

Lincoln suffered losses totaling $24.2 million on the HPLP transaction. Lincoln also incurred losses of over $12.2 million on the ESOP transaction. In total, Lincoln suffered substantial losses, in excess of $36 million, on the transactions at issue in this proceeding.

F. Grounds Exist For The Entry Of An Industry-wide Prohibition Order Against Respondent

Keating participated in violations of the FSLIC affiliated persons regulations and transactions with affiliates law and regulations, engaged in unsafe and unsound practices, and committed breaches of his fiduciary duties, including engaging in impermissible conflicts of interest. Respondent's violations, conduct and practices with respect to Lincoln and ACC caused Lincoln to suffer substantial financial loss within the meaning of former section 407(g)(2) of the NHA, 12 U.S.C. § 1730(g)(2) (1988).

In addition, Respondent acted with "willful disregard" and "continuing disregard" for the safety and soundness of Lincoln, and Respondent's conduct and practices evidence his unfitness to participate in the conduct of the affairs of Lincoln or any other insured institution, within the meaning of former section 407(g)(2) of the NHA, 12 U.S.C. § 1730(g)(2) (1988).[42] Accordingly, the Acting Director, pursuant to his authority under section 8(e) of the FDIA, will prohibit Keating from participating in any manner in the conduct of the affairs of any insured depository institution or any other entity listed in section 8(e)(7) of the FDIA. 12 U.S.C. § 1818(e)(7).[43]

1. Willful or Continuing Disregard for the Safety and Soundness of Lincoln

Keating, as a controlling person of Lincoln, acted with willful disregard[44] for the safety and soundness of Lincoln by

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42. Respondent's conduct would also warrant the imposition of a prohibition order under section 8(e) of the FDIA, 12 U.S.C. § 1818(e). Keating, an institution-affiliated party of Lincoln, violated laws and regulations, engaged and participated in unsafe and unsound practices and breached his fiduciary duty; by reason of such violations, practices and breaches, Lincoln suffered loss and Keating received financial gain and other benefit; and such violations, practices and breaches demonstrate willful and continuing disregard for the safety and soundness of Lincoln.

43. Furthermore, by virtue of his federal and state criminal convictions for crimes involving dishonesty and/or breaches of trust, Keating, by operation of statute, is prohibited from employment, ownership and all other activities which constitute direct or indirect participation in the affairs of any insured depository institution, which institutions include, but are not limited to, banks, savings associations and credit unions. 12 U.S.C. §§ 1785 (1988 & Supp. IV 1992) and 1829 (Supp. IV 1992). Sections 1785 and 1829 provide for a fine of not more than $1 million for each day the prohibition is knowingly violated and/or imprisonment for not more than 5 years. 12 U.S.C. §§ 1785, 1829.

44. Willful disregard occurs when an individual

> (a) purposely (as opposed to accidentally) commits an act and that act evidences neglect or lack of thoughtful attention to the institution's safety or soundness, or (b) acts with plain indifference to the institution's safety and soundness. . . . [T]he only requirement is that the individual acted intentionally in committing the acts which constitute the violation and was aware of or knew what he was doing.

causing, bringing about and participating in the advance and extension of credit to HPLP even though he knew that such advance and extension of credit were prohibited affiliated persons transactions. Findings ¶¶ 31, 65. The advance and extension of credit were highly imprudent. Respondent's conduct reflected neglect for, a lack of thoughtful attention and plain indifference to Lincoln's safety and soundness.

Respondent acted with willful disregard for the safety and soundness of Lincoln by entering into the FRESOP note transaction which required a pledge and guarantee by Lincoln, when he knew that such a pledge and guarantee were prohibited under transactions with affiliates and affiliated persons regulations. Findings ¶¶ 95-100, 172-81.

In addition, after being informed that Lincoln's pledge and guarantee violated transactions with affiliates and affiliated persons law and regulations, Respondent took no steps to undo Lincoln's pledge and guarantee and willfully allowed the pledge to remain in effect for over three years until the notes went into

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(Footnote 44 continued from previous page)
In the Matter of M, at 51. See also In the Matter of Kim, Final Decision and Order, OTS Order No. AP 93-30 (April 30, 1993) (appeal pending); In the Matter of O'Keeffe, Decision and Order, FHLBB Res. No. 89-773, 28-29 (April 26, 1990).

default. Findings ¶¶ 187-96. This pattern of conduct demonstrates continuing disregard[45] for Lincoln's safety and soundness.

2. Unfitness to Participate in the Conduct of the Affairs of Lincoln Or Any Insured Institution

Respondent manipulated Lincoln for his personal financial benefit in breach of his fiduciary responsibilities as a controlling shareholder and with reckless disregard for applicable laws and regulations and willful and continuing disregard for the safe and sound operations of Lincoln and its depositors. Respondent's conduct and practices with respect to Lincoln and ACC, including: engaging in a convoluted scheme to finance the purchase of the Hotel by HPLP, such that there was no loan directly from Lincoln or its subsidiaries to HPLP in order to avoid the regulations restricting loans to affiliated persons; allowing the advance and extension of credit to HPLP with the knowledge that such loans would violate affiliated persons regulations; proceeding with the ESOP transaction with the understanding, based upon experiences with an earlier loan to the ESOP, that applicable regulations restricted the manner in which Lincoln could make loans and extend credit to its affiliates and affiliated persons; and the failure to take any steps to correct or undo Lincoln's pledge, or to substitute collateral other than that of Lincoln to secure the ESOP financing, after becoming aware, through a FHLBB opinion letter and discussions with counsel, that Lincoln's pledge of

45. "Continuing disregard" requires "some showing of knowledge of wrongdoing, [but] it does not require proof of the same degree of intent as 'willful disregard'." Brickner v. FDIC, 747 F.2d 1198, 1203 (8th Cir. 1984); In the Matter of Kim, at 23; In the Matter of M, at 50; In the Matter of O'Keeffe, at 28.

collateral for the ESOP's obligation violated laws and regulations; clearly evidence his unfitness to participate in the affairs of Lincoln or any insured depository institution.

IV. RESPONDENT'S REQUEST FOR ORAL ARGUMENT

Included in Respondent's exceptions to the Recommended Decision and his May 13, 1993 reply was a request for oral argument before the Director or a rehearing.[46] Enforcement Counsel opposed this request. Under the OTS's administrative procedural regulations, the Director has the discretion to order and hear oral argument. However, a party seeking oral argument has the burden of showing good cause for such argument, including reasons why arguments have not been, or cannot be, presented adequately in writing. 12 C.F.R. § 509.30 (1991). Upon consideration of Respondent's request for oral argument, Enforcement Counsel's opposition, the allegations and arguments presented in the parties' filings and the many opportunities Respondent has been afforded to present his arguments, the Acting Director finds that: (1) at every opportunity, Respondent has failed to set forth his legal arguments in written submissions; (2) the Acting Director will not be aided in deciding this matter by oral argument; and (3) Respondent will not be prejudiced by the lack of oral argument. Therefore, the Acting Director declines to exercise his discretion under section 509.30 of the OTS's rules and denies Respondent's

46. Keating asserted that he has not had an adequate opportunity to be heard in the proceeding.

request for oral argument. For these same reasons, the Acting Director denies Respondent's alternate request for a rehearing.

V. CONCLUSIONS

For the reasons set forth above, the Acting Director concludes that Respondent's participation in the HPLP and ESOP transactions warrant the issuance of an order requiring Keating to cease and desist from the violations and practices involved in this proceeding and to make restitution to Lincoln for the losses suffered, $36.4 million.[47]

The Acting Director further concludes that Respondent's violations, practices and breaches of his fiduciary duty warrant prohibiting Keating from participating in the conduct of the affairs of any insured depository institution or any other institution or entity listed in section 8(e)(7) of the FDIA.

The Acting Director does not affirm the ALJ's findings of liability against Kielty. Since the filing of the ALJ's Recommended Decision, Kielty consented to the issuance of a cease

47. This amount does not include a prejudgment interest component that was included in the restitution amount suggested in the ALJ's Recommended Decision. Prejudgment interest is not assessed because Enforcement Counsel did not ask for such amounts in the Notice of Charges, the Amended Notice or in any other filings in the proceeding except in Enforcement Counsel's proposed findings of fact and conclusions of law, and failed to provide a legal basis for the imposition of prejudgment interest.

and desist order without admitting or denying the assertions in the Notice of Charges. OTS Order No. AP 93-63 (July 16, 1993).

ORDER

Upon consideration of the entire record in this matter, including the Recommended Decision of the Administrative Law Judge and the exceptions to the Recommended Decision filed by Keating, Enforcement Counsel's response to Keating's exceptions and Keating's reply thereto, and for the reasons set forth in the accompanying Decision:

The Acting Director, pursuant to his authority under 12 U.S.C. § 1818(b) (Supp. IV 1992), and former section 407(e) of the NHA, 12 U.S.C. § 1730(e) (1988), finds that: Charles H. Keating, Jr., in his former capacity as Chairman of the Board and controlling shareholder of ACC at all relevant times, in his former capacity as President and Chief Executive Officer of ACC from September 1981 through May 1985, and by his control over Lincoln, was an institution-affiliated party of Lincoln and a person participating in the conduct of the affairs of Lincoln who violated laws and regulations including 12 U.S.C. § 1730a(d) (1988) and 12 C.F.R. §§ 563.43, 584.3 and 526.23-3 (1985), and engaged in unsafe and unsound practices, including breaches of his fiduciary duties to Lincoln, including those defined in 12 C.F.R. § 571.7 (1985), in conducting the business of Lincoln. Keating was unjustly enriched in connection with these violations and practices, and the violations and practices involved reckless disregard for the law and applicable regulations. Accordingly, grounds exist under 12

U.S.C. § 1818(b) to issue a cease and desist order requiring affirmative action to correct or remedy conditions resulting from these violations and practices.

The Acting Director, pursuant to his authority under 12 U.S.C. § 1818(e) (Supp. IV 1992) and former section 407(g) of the NHA, 12 U.S.C. § 1730(g) (1988), finds that: Keating, in his capacity specified above, violated laws and regulations including 12 U.S.C. § 1730a(d)(1988) and 12 C.F.R. §§ 563.43, 584.3 and 526.23-3 (1985), engaged and participated in unsafe and unsound practices in connection with Lincoln, and committed and engaged in acts, omissions and practices that constitute breaches of his fiduciary duties to Lincoln, including those defined in 12 C.F.R. § 571.7 (1985), as a controlling shareholder of the institution. By reason of such conduct, violations, practices and breaches, Lincoln has suffered substantial financial loss or other damage, and Keating has received financial gain or other benefit. Keating's conduct, violations, practices and breaches involved willful or continuing disregard for the safety and soundness of Lincoln, and evidence his unfitness to participate in the conduct of the affairs of Lincoln or any other insured depository institution. Accordingly, grounds exist to issue an order prohibiting Keating from further participation in the conduct of the affairs of Lincoln, its successors, any of its subsidiaries, and all other institutions and entities listed in 12 U.S.C. § 1818(e)(7).

IT IS, THEREFORE, HEREBY ORDERED that:

1. The ALJ's Recommended Decision, a copy of which is attached hereto as Attachment A, is hereby affirmed, except insofar as it is inconsistent with this Final Decision and Order; and the ALJ's findings of fact and conclusions of law with respect to Keating's liability, which are attached to the ALJ's Recommended Decision as Appendix A and Appendix B, respectively, are hereby adopted as the Acting Director's findings of fact and conclusions of law and incorporated herein by reference.

2. Keating shall cease and desist from engaging in any acts, omissions, or practices involving unsafe or unsound practices, and violations of law or regulations;

3. Within ten (10) business days after the effective date of this Order, Keating shall pay restitution in the amount of Thirty-six million, three hundred ninety-eight thousand, seven hundred thirty-eight dollars and seventy-six cents ($36,398,738.76), to Lincoln, in receivership, in a form acceptable to the Resolution Trust Corporation ("RTC") as receiver;

4. The RTC's failure, for any reason, to approve the form of restitution by Keating shall not relieve Keating of his obligation to pay restitution to Lincoln pursuant to this Decision and Order;

5. Keating is prohibited from further participation, in any manner, in the conduct of the affairs of Lincoln, its successors, or any of its subsidiaries pursuant to 12 U.S.C. § 1818(e);

6. While this Order is in effect, Keating shall not continue or commence to hold any office in, or participate in any manner in the conduct of the affairs of, any institution or entity listed in 12 U.S.C. § 1818(e)(7)(A);

7. Conduct prohibited by this Order includes the conduct specified under 12 U.S.C. § 1818(e)(6);

8. This Order is subject to the provisions of 12 U.S.C. § 1818(j);

9. The provisions of this Order are effective as to Keating upon the expiration of thirty (30) days after service of this Order upon him and shall remain effective and enforceable, except to the extent that, and until such time as, any provisions of this Order shall have been stayed, modified, terminated, or set aside by action of the Acting Director or a reviewing court, or in accordance with 12 U.S.C. § 1818(e)(7)(B);

IT IS FURTHER ORDERED that:

10. Keating's request for oral argument or rehearing is denied; and

11. Keating is hereby notified that he has the right to appeal this Final Decision and Order to the United States Court of Appeals within 30 days after the date of service of such Final Decision and Order. 12 U.S.C. § 1818(h).

THE OFFICE OF THRIFT SUPERVISION

Dated: 10/22/93

By: /S/
Jonathan L. Fiechter
Acting Director