UNITED STATES OF AMERICA
Before the
OFFICE OF THRIFT SUPERVISION

In the Matter of		
NEIL M. BUSH		
A Former Director of Silverado Banking, Savings and Loan Association, Denver, Colorado	)	Enforcement Review Committee Resolution No. ERC-90-30 OTS AP 91-16

ORDER TO CEASE AND DESIST

For the reasons set forth in the attached Decision of the Director of the Office of Thrift Supervision in the above-captioned matter, the Director of the Office of Thrift Supervision, as successor to the Federal Savings and Loan Insurance Corporation pursuant to section 401(f) of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183, 356 ("FIRREA"), and section 3 of the Home Owners' Loan Act, as amended by section 301 of FIRREA, 103 Stat. at 278-80, finds that Respondent, Neil M. Bush, in his former capacity as a director of Silverado Banking, Savings and Loan Association, Denver, Colorado, has engaged in unsafe or unsound practices and breaches of his fiduciary duties involving multiple conflicts of interest. This conduct was contrary to generally accepted standards of prudent operation of an insured depository institution and its possible consequence, if continued, may be abnormal risk, or loss, or damage to an institution, its shareholders, or the federal deposit insurance funds. Accordingly, grounds exist to issue a cease and desist order under section 407(e) of the National Housing Act ("NHA") (12 U.S.C. § 1730(e)(1) (1988)), now repealed and superseded by section 902 of FIRREA (to be codified at 12 U.S.C. § 1818(b)(1)).

Pursuant to his authority under section 8(b) of the Federal Deposit Insurance Act ("FDIA") to issue an order pursuant to this cease and desist proceeding, the Director

HEREBY ORDERS that:

1. Respondent, Neil M. Bush, cease and desist from any acts, omissions, or practices involving any conflicts of interest, unsafe or unsound practices, or breaches of fiduciary duties, as defined in 12 C.F.R. § 571.7, or any successor statutes or regulations, and as established by the common law and discussed in the attached Decision.

2. Upon becoming affiliated with a federally insured depository institution, or any holding company thereof, Respondent shall:

(a) obtain advice of competent counsel on his duties and responsibilities, both initially upon accepting such a position and when particular issues arise that may cause Respondent to be uncertain about his responsibilities;

(b) abstain from voting or participating in any manner on any proposals in which Respondent has a personal interest and may experience a direct or indirect benefit;

(c) in connection with any transaction subject to subparagraph (b), make full disclosure of the existence of Respondent's interest and its nature and extent, and of the facts known to Respondent as to the matter or transaction under consideration;

(d) at least annually, and with a continuing obligation in the event of a change of circumstances, make full disclosure of any and all loans, investments, partnership interests, stock ownership, and any other business relationships, which constitute a conflict of interest as defined in 12 C.F.R. § 571.7 (as well as any successor statutes and regulations), the attached Decision, and the common law, with persons who are customers or prospective customers of such institution or its affiliates; and

(e) refrain generally from violating the standard governing conflicts of interest, fiduciary duties, and safe or sound operations, as set forth in 12 C.F.R. § 571.7 (as well as any successor statutes and regulations), the attached Decision, and the common law.

3. This Order shall become effective at the expiration of thirty (30) days after it is served upon Respondent.

THE OFFICE OF THRIFT SUPERVISION

By: /S/
Timothy Ryan
Director

Date: April 18, 1991

UNITED STATES OF AMERICA

Before the

OFFICE OF THRIFT SUPERVISION

In the Matter of **NEIL M. BUSH** **A Former Director of Silverado Banking, Savings and Loan Association, Denver, Colorado**	)	**Enforcement Review Committee Resolution No. ERC-90-30**

DECISION AND ORDER

April 18, 1991

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DECISION

I. INTRODUCTION AND SUMMARY OF CONCLUSIONS

No activity is more critical to the survival and success of any insured financial institution than the faithful performance by its officers and directors of their fiduciary duties. By their efforts, the institution operates; only through their diligence, loyalty, care, and candor may it prosper. Failure of a director to satisfy these fiduciary duties undermines the foundation of an institution's safe and sound operation. For this reason, a director's adherence to his fiduciary duties must be an obligation keenly appreciated and scrupulously followed. This is a case where a director failed to meet these standards.

Mr. Neil M. Bush ("Respondent") was a director of Silverado Banking, Savings and Loan Association (the "Association"). At a time when the Association's board of directors was considering purchases of property from, and loans to, entities owned or controlled by Bill L. Walters ("Walters"), Respondent failed to disclose to the Association's board that Walters was a limited partner in JNB Exploration Company ("JNBE"), Respondent's primary business and source of income, that JNBE was indebted to Walters, and that JNBE and Respondent were obligated to Cherry Creek National Bank ("CCNB"), of which Walters was the controlling

shareholder. Respondent voted as a board member to approve the transactions with the Walters entities.

Respondent also failed to disclose to the board his relationships with another business associate, Kenneth M. Good ("Good"), and his interest in transactions involving Good that were being considered by the Association's board of directors.

In his recommended decision and order, the Administrative Law Judge ("ALJ") found that Respondent had failed to disclose these matters when various transactions were being considered by the board of directors of the Association. The ALJ concluded that this conduct involved significant conflicts of interest and constituted multiple breaches of Respondent's fiduciary duties to the Association and unsafe and unsound practices that could conceivably be repeated at other federally regulated institutions. Accordingly, the ALJ recommended that the Office of Thrift Supervision ("OTS") issue against Respondent an order to cease and desist from such conflicts of interest in the future.

The Director of the OTS ("Director") concludes that a director of an insured depository institution who may experience a direct or indirect benefit in connection with a matter before a board of directors, has a conflict of interest and therefore would breach his fiduciary duties if he fails to disclose to the

board of directors all material nonprivileged information relevant to the board's decision on the matter, or if he participates in the matter, or if he votes on it.

The Director agrees with the ALJ's conclusions and finds that Respondent breached his fiduciary duties of candor and loyalty and engaged in unsafe or unsound practices in his capacity as a member of the board of directors of a federally insured depository institution. The conduct was clearly contrary to generally accepted standards of prudent operation of a financial institution. Where a director breaches his fiduciary duties, the soundness of the institution's management function is impaired. Thus, the possible consequence of such conduct, if continued, may be abnormal risk, or loss, or damage to an insured financial institution, its shareholders, or the deposit insurance fund. Accordingly, the Director concludes that a cease and desist order should be issued against Respondent.

In view of the Director's conclusions, the attached Order requires Respondent to cease and desist from any acts, omissions, or practices involving any conflicts of interest, unsafe or unsound practices, or breaches of fiduciary duties, as defined in 12 C.F.R. § 571.7, the common law, and the discussion that follows in this Decision. In addition, if Respondent becomes an institution-affiliated party in the future, the Order requires him to obtain advice of counsel as to his responsibilities;

abstain from voting or participating in any manner on proposals in which he has a personal interest and may experience a direct or indirect benefit; make full disclosure of his interest in such proposals; at least annually disclose any conflicts of interest; and generally refrain from violating standards governing conflicts of interest, fiduciary duties, and safe and unsound operations.

II. BACKGROUND

A. Charges Against the Respondent

This matter arises from a Notice of Charges and Hearing filed on February 5, 1990, and amended pursuant to the ALJ's Order of October 5, 1990.[1] The Notice alleges that, during his

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[1] This cease and desist action was initiated by the Office of Enforcement ("Enforcement") of the OTS against Respondent, a former director of the Association, for alleged breaches of fiduciary duties involving conflicts of interest and unsafe or unsound practices. The Association was a Colorado savings association with accounts insured by the former Federal Savings and Loan Insurance Corporation ("FSLIC") pursuant to section 403(b) of the National Housing Act, 12 U.S.C. § 1726(b) (1988) ("NHA"). The Association failed and was placed in receivership by the FSLIC on December 16, 1988.

Until August 9, 1989, the Federal Home Loan Bank Board ("FHLBB") was the operating head of the FSLIC. On August 9, 1989, President Bush signed into law the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 ("FIRREA"). FIRREA abolished both the FHLBB and the FSLIC, and created the OTS.

Section 3 of the Home Owners' Loan Act ("HOLA"), as amended by FIRREA, provides that the Director succeeds to the powers that had been vested in the FHLBB. 103 Stat. at 278 (to be codified at 12 U.S.C. § 1462a(e)). Section 401(f) of FIRREA further provides that the abolition of the FSLIC does not affect the validity of FSLIC's rights under any section of title IV of the National Housing Act. 103 Stat. at 356. Thus, the Director

tenure as a director from August 1985 to August 1988, Respondent failed to disclose certain information to the Association's board of directors, and as a result, breached his fiduciary duties to the Association and engaged in unsafe or unsound practices. Three separate instances of failure to disclose form the basis for the Notice.

First, the Notice alleges that Respondent failed to disclose his business relationships with Walters or his personal and business obligations to CCNB, of which Walters was the controlling shareholder, and that Respondent failed to disclose that JNBE was indebted to Walters. Subsequently, Respondent voted to approve purchases of property from, and loans made to, Walters or entities Walters owned or controlled. As a result, the Notice contends, Respondent breached his fiduciary duty to the Association and engaged in an unsafe or unsound practice by voting to approve transactions with and loans to entities owned or controlled by one of his business partners or creditors.

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succeeds FSLIC as the party-in-interest and may proceed against Respondent pursuant to section 407(e) of the NHA, which was repealed by FIRREA and superseded by section 8(b) of the Federal Deposit Insurance Act ("FDIA"), as amended by FIRREA. 12 U.S.C. § 1730(e); 103 Stat. at 450 (to be codified at 12 U.S.C. § 1818(b)). FIRREA repealed section 407(e) of the NHA, but the grounds for issuance of a cease and desist order set forth in the NHA still govern actionable conduct that occurred before that statute's enactment. Post-FIRREA, the OTS's authority to issue a cease and desist order is derived from section 8(b) of the FDIA.

Secondly, the Notice alleges that Respondent failed to disclose adequately his personal indebtedness to Good or his business relationships with Good. On Good's behalf, Respondent sought a $900,000 line of credit from the Association to enable Respondent's business enterprise, acting in partnership with Good, to bid on oil and gas concessions in Argentina. According to the Notice, Respondent breached his fiduciary duty to the Association and engaged in an unsafe or unsound practice by attempting to bring about a transaction that, if consummated, would have resulted in benefit to himself; and by attempting to bring about the execution of a line of credit that, if made, would have violated the regulation prohibiting transactions with affiliates at 12 C.F.R. § 563.43(b). The Notice also asserts that Respondent breached his fiduciary duty to the Association and engaged in an unsafe or unsound practice by failing to make adequate disclosure of the nature of the proposed transaction and his interest in it.

Finally, the Notice alleges that Respondent breached his fiduciary duty to the Association and engaged in an unsafe or unsound practice by failing to disclose to his fellow directors an agreement contemplating Good's contribution of over $3 million to Respondent's partnership, at a time when the other directors were considering a substantial release of collateral and forgiveness of debt on Good loans at the Association.

B. <u>Proceedings Below</u>

Following a hearing during which the parties presented the testimony of witnesses and introduced documentary evidence, Administrative Law Judge Daniel J. Davidson (the "ALJ") issued his Recommended Decision, Recommendation, and Recommended Order to Cease and Desist ("Recommended Decision") on December 17, 1990. On January 7, 1991, Enforcement filed an exception to the ALJ's recommended cease and desist order; on January 27, 1991, Respondent filed exceptions to both the ALJ's decision and order. On February 11, 1991, the parties were notified that the ALJ's Recommended Decision had been submitted for the Director's review and final administrative determination. <u>See</u> 12 C.F.R. § 509.32(b).

C. <u>The ALJ's Recommended Decision and Order</u>

The ALJ made numerous findings of fact and conclusions of law leading to his ultimate conclusion that Respondent had engaged in unsafe or unsound practices involving multiple conflicts of interest that could conceivably be repeated at other federally regulated institutions, and that this conduct necessitated the imposition of an order to cease and desist from all future such conflicts and practices.

The ALJ concluded that Respondent, by voting to approve the Walters transactions without full disclosure to the board of

directors, had engaged in conduct that violated the Association's internal policy on conflicts of interest and involved a significant conflict of interest constituting an inherently unsafe or unsound practice as defined in 12 C.F.R. § 571.7.

The ALJ further determined that Respondent's failure to disclose fully to the board of directors his close business relationship with Good and his own interest in the proposed $900,000 line of credit to Good's company involved conduct that violated the Association's internal policy and involved a significant conflict of interest constituting an inherently unsafe or unsound practice as defined in section 571.7.

Similarly, the ALJ found that Respondent's failure to disclose to the board of directors the full nature and extent of his relationship with Good and all the information available to him concerning Good's financial condition at the time the Good loan modification was being considered by the board violated the Association's internal policy and involved a significant conflict of interest constituting an inherently unsafe or unsound practice as defined in section 571.7.

The recommended order to cease and desist would require Respondent to cease and desist from any acts, omissions, or practices involving conflicts of interest as defined in section 571.7 or involving a breach of fiduciary duty to any federally

insured depository institution. The ALJ also recommended that the Director order Respondent to cease any unsafe or unsound practice as an institution-affiliated party.

The ALJ further suggested that, upon becoming an officer, director, or controlling person of a federally insured depository institution, Respondent be required to obtain advice of competent legal counsel on his duties and responsibilities; abstain from voting or participating in any proposals involving persons or business entities in which Respondent has any interest; and at least annually make full disclosure of all business relationships with institution customers or prospective customers, as well as any business relations with a party who has a proposed transaction before the institution's board. The ALJ also recommended that Respondent be ordered not to violate conflict of interest laws, regulations, and policy statements and to take any affirmative action necessary to correct any conditions resulting from violation of the order.

D. Exceptions to the ALJ's Recommended Decision

Respondent raised numerous exceptions to the ALJ's findings of fact. The Director has adopted the ALJ's findings of fact with certain minor modifications based on the Director's rulings on Respondent's exceptions. The Director's findings are set forth in the Appendix to this Decision, which also contains a brief discussion of the disposition of Respondent's exceptions to

the ALJ's findings of fact.

Respondent excepts to the conclusions of law on the grounds that: (1) the OTS failed to meet the standard necessary to support a cease and desist order; (2) section 571.7 is unconstitutionally vague and does not establish a standard of conduct; (3) the ALJ's findings fail to establish that Respondent violated section 571.7; and (4) Respondent did not breach his fiduciary duties on any of the occasions alleged by the OTS. Respondent also argues that the ALJ failed to exercise independent judgment in reaching his recommended decision. These points are discussed in section III of this Decision. The Director has concluded that the ALJ's findings and conclusions, as modified herein, support the issuance of a cease and desist order against Respondent.

Enforcement filed one exception to the recommended order to cease and desist. Enforcement seeks an order requiring Respondent to demonstrate, prior to assuming a position as an institution-affiliated party, the ability to recognize and respond to actual and potential conflicts of interest. For the reasons described below, the Director denies this exception.

III. DISCUSSION

A. The Standard of Conduct Applicable to Thrift Directors

Directors of a savings association have a fundamental duty

to avoid placing themselves in a position that creates, or that leads to or could lead to, a conflict of interest or appearance of a conflict of interest. This standard, which appears in an FHLBB (now OTS) statement of policy, 12 C.F.R. § 571.7,[2] restates a fundamental fiduciary obligation of directors of any corporate entity -- one that should be felt even more strongly by directors and officers of depository institutions. These directors owe an

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[2] Respondent contends that section 571.7 is unconstitutionally vague as applied by the ALJ and that "a regulation is unconstitutionally vague when it either forbids or requires the doing of an act in terms so vague that men of common intelligence must necessarily guess at its meaning and differ as to its application." To bolster his argument, Respondent inappropriately cites cases involving constitutionally protected rights. These cases are not applicable where the regulation at issue does not involve a criminal prosecution or a constitutionally protected activity. See Brennan v. Occupational Safety & Health Review Comm'n, 505 F.2d 869, 872 (10th Cir. 1974).

To the extent the courts consider the vagueness doctrine at all in the context of economic regulation, they consistently hold that economic regulation is subject to a less stringent vagueness analysis. "Economic regulation usually deals with a narrower subject and those affected by it are more likely to consult the law, seeking clarification if necessary, in order to plan their behavior." Brockert v. Skornicka, 711 F.2d 1376, 1381 (7th Cir. 1983). See also Village of Hoffman Estates v. The Flipside, Hoffman Estates, Inc., 455 U.S. 489, 494-95, reh'g denied, 456 U.S. 950 (1982); Exxon Corp. v. Busbee, 644 F.2d 1030, 1033 (5th Cir.), cert. denied sub nom. Exxon Corp. v. Georgia Ass'n of Petroleum Retailers, 454 U.S. 932 (1981). The rigorous application of a vagueness analysis as urged by Respondent is especially inappropriate in the context of a banking regulation. As discussed in the text below, content may be given to the unsafe or unsound concept through the evolution of agency practice.

Section 571.7 imposes no criminal penalty and involves no constitutionally protected right. Its meaning is sufficiently clear. Therefore, the Director rejects Respondent's argument that section 571.7 is unconstitutionally vague.

even higher fiduciary duty to the institutions they serve than do directors of other companies. Because they are obliged to safeguard depositors' money, depository institution directors are held to "standards of probity and fidelity more lofty than those of 'the market place.'" Fleishhacker v. Blum, 109 F.2d 543, 547 (9th Cir.), cert. denied, 311 U.S. 655, reh'g denied, 311 U.S. 726 (1940).[3]

The substance of a director's fiduciary duty to a federally insured, state-chartered savings association is established by federal as well as state statute and common law.[4] State law does

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[3] See also Briggs v. Spaulding, 141 U.S. 132, 147, 152 (1891); Gadd v. Pearson, 351 F. Supp. 895, 903 (M.D. Fla. 1972); FSLIC v. Huff, 704 P.2d 372, 378 (Kan. 1985). Accordingly, officers and directors of depository institutions are held to a strict fiduciary duty to act in the best interests of the institution, its shareholders and its depositors. See, e.g., Lane v. Chowning, 610 F.2d 1385, 1388-89 (8th Cir. 1979); First Nat'l Bank of La Marque v. Smith, 436 F. Supp. 824, 831 (S.D. Tex. 1977), aff'd in part and vacated in part on other grounds, 610 F.2d 1258 (5th Cir. 1980); Ringeon v. Albinson, 35 F.2d 753, 754 (D. Minn. 1929); Francis v. United Jersey Bank, 432 A.2d 814, 821 (N.J. 1981); Litwin v. Allen, 25 N.Y.S.2d 667, 678 (N.Y. Sup. Ct. 1940); 3 W. Fletcher, Cyclopedia of the Law of Private Corporations § 838 (rev. perm. ed. 1986).

[4] See, e.g., Bowerman v. Hamner, 250 U.S. 504, 510 (1919) (duty of care of national bank director is imposed both by National Bank Act and under common law arising from director's fiduciary relationship to stockholders and depositors); Briggs v. Spaulding, 141 U.S. 132, 146, 152 (1891) (duty of care of national bank director under National Bank Act and common law); Hoye v. Meek, 795 F.2d 893, 896 (10th Cir. 1986) (director violated state banking statute codifying duty of care); Hoehn v. Crews, 144 F.2d 665, 672, 673 (10th Cir. 1944), aff'd sub nom. Garber v. Crews, 324 U.S. 200 (1945) (fiduciary duties of national bank director arising under statute and common law); Fleishhacker v. Blum, 109 F.2d 543, 547 (9th Cir.), cert. denied, 311 U.S. 655, reh'g denied, 311 U.S. 726 (1940) (common law duty of loyalty of national bank officer); FSLIC v. Olano, No. 86-472,

not provide the exclusive statement of the fiduciary duties of directors of a federally insured institution. The federal government as regulator and insurer has a compelling interest in establishing a uniform nationwide minimum standard of conduct, and to that end may establish a regulatory and common law of fiduciary duties that does not depend on the location of the institution. Bricker v. FDIC, 747 F.2d 1198, 1202 (8th Cir. 1984); Beverly Hills Fed. Savings & Loan Ass'n v. FHLBB, 371 F. Supp. at 314.

A fundamental component of the fiduciary duties of directors in every jurisdiction, however, is that directors owe a duty of loyalty to the institution they serve. This duty prohibits directors from engaging in transactions that involve conflicts of interest with the institution.[5] When faced with divided

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slip op. at 1, 10-13 (E.D. La. May 17, 1989) (federal thrift's directors and officers breached duties of care and loyalty established under federal common law); Beverly Hills Fed. Savings & Loan Ass'n v. FHLBB, 371 F. Supp. 306, 313, 314, 316-17 (C.D. Cal. 1973) ("federal regulatory scheme . . . [embraces] fundamental principles of the common law consistent with policies of the regulatory scheme and necessary for their implementation"; federal thrift's controlling shareholders held to have breached their common law fiduciary duties even if their conduct did not violate any specific regulation of FHLBB); Goodman v. Perpetual Building Ass'n, 320 F. Supp. 20, 38 (D.D.C. 1970) (common law duty of loyalty of state-chartered thrift director).

[5] First Nat'l Bank of La Marque v. Smith, 436 F. Supp. at 829; see United States v. Byrum, 408 U.S. 125, 137-38 (1972) (controlling person cannot abuse his power by promoting his interests at the expense of the corporation's interest); Pepper v. Litton, 308 U.S. 295, 306, 310-11 (1939) (a director is a fiduciary and equity will not permit a fiduciary to use his power for his personal advantage); 12 C.F.R. §§ 571.7, 571.9; FHLBB Memorandum R 62. Congress has directly recognized the serious

loyalties, directors must demonstrate both their good faith and the inherent fairness to the corporation of transactions in which they have a financial, business or other personal interest. Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1280 (Del. 1989).

Subsumed within the fiduciary duty of loyalty is the duty of candor. This duty requires that corporate fiduciaries "disclose all material information relevant to corporate decisions from which they may derive a personal benefit." Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d at 1280. See Beverly Hills Fed. Savings & Loan Ass'n v. FHLBB, 371 F. Supp. at 314 (savings association's control group breached their fiduciary duties to the institution's members in transferring control of the thrift without complete disclosure to the members); Brickner v. FDIC, 747 F.2d at 1200, 1202 (bank directors' failure to stop a fellow director's improper practices was a breach of their fiduciary duties and ground for a removal order); Weinberger v. UOP, Inc., 457 A.2d 701, 709, 710 (Del. 1983) (inside directors' failure to disclose price feasibility study to outside directors in connection with a cash-out merger was a breach of their fiduciary duties). See also In Re: Illinois Valley Acceptance Corp., 531 F. Supp. 737, 741 (C.D. Ill. 1982) (director held liable for

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consequences of self-dealing to the health of financial institutions. H.R. Rep. No. 1383, 95th Cong., 2d Sess. 10, reprinted in 1978 U.S. Code Cong. & Admin. News 9273, 9282.

failing to disclose another director's conflict of interest).

Colorado law similarly and unequivocally establishes that directors owe duties of good faith and loyalty to their corporations and shareholders. Kullgren v. Navy Gas & Supply Co., 135 P.2d 1007, 1010 (Colo. 1943). The specific duties to which Colorado courts have held directors include:

> (1) Not to profit at the expense of the corporation or shareholders, (2) not to speculate with corporate property or use corporate property or their relation to it for personal gain, (3) not to secure a private advantage through the use of official powers at the expense of the corporation, and (4) not to deal with corporate property in a personal transaction without the approval of the shareholders.

De La Garza, Conflict of Interest Transactions: Fiduciary Duties of Corporate Directors Who Are Also Controlling Shareholders, 57 Denver Law Journal 609, 612-13 (1980) (citations omitted).[6]

The threshold inquiry in assessing whether a director violated his duty of loyalty is whether the director has a conflicting interest in the transaction. Directors are considered to be "interested" if they either "appear on both sides of a transaction []or expect to derive any personal financial benefit from it in the sense of self-dealing, as opposed to a benefit which devolves upon the corporation or all

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[6] Decisions in other states are generally in accord. See, e.g., Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1986); Weinberger v. UOP, Inc., 457 A.2d 701, 710 (Del. 1983); Guth v. Loft, Inc., 5 A.2d 503, 510 (Del. 1939).

stockholders generally." Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) (emphasis added); see D. Block, N. Barton & S. Radin, The Business Judgment Rule: Fiduciary Duties of Corporate Directors 15 (3d ed. 1989).

The conflicting interest need not be a direct financial one. For example, in Drobbin v. Nicolet Instrument Corp., 631 F. Supp. 860 (S.D.N.Y. 1986), the Southern District of New York held that a conflict of interest might arise less directly:

> Such are the subtleties of human relationships that self-dealing and conflicts of interest may take many forms. "The conflict of interest of a director may arise not only out of one's personal business interests or one's directorship in another corporation; it may also stem from a desire to favor friends, relatives, or business associates."

Id. at 879 (emphasis added; citations omitted). The court further stated that a director not "financially interested" in a transaction may nevertheless "forfeit the savings status of 'independent director' for more subtle, less direct entanglements and alliances." Id. at 881.[7]

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[7] The facts involved a director who voted to approve a corporate transaction with another company. Although he had no direct financial interest in the specific transaction or in the other company, he did have a business relationship with another director who was financially interested in the transaction. The court found he had an interest in enjoying the good will of the other interested director, and was "entirely dependent upon [the other director] for an entree into the practice of law . . . ." Id. at 881-82. Accordingly, the court held that the director had a prohibited conflict of interest. See also Borden v. Sinskey, 530 F.2d 478, 495 (3d Cir. 1976) ("[w]hile a showing of financial interest is certainly relevant to, and often dispositive of, this question [of director interest], it is only one factor to be considered by the finder of fact"; directors not disinterested

The duty of candor requires that "directors 'protect the rights of the company and act openly and above board.'" Great Western United Corp. v. Great Western Producers Cooperative, 588 P.2d 380, 382 (Colo. Ct. App. 1978), quoting Sprague v. Stratton-Massachusetts Gold Mines Co., 125 P. 490, 491 (Colo. 1912). This obligates a director to share with the other board members such information as he may possess that bears on a transaction under consideration by the board.

Corporate fiduciaries, of course, also must disclose completely all material information relevant to corporate decisions from which they may derive a personal benefit. Rosenblatt v. Getty Oil Co., 493 A.2d 929, 937, 944 (Del. 1985); Weinberger v. UOP, Inc., 457 A.2d 701, 711 (Del. 1983); Rosenthal v. Four Corners Oil & Minerals Co., 403 P.2d 762, 766 (Colo. 1965). See also TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976); Goss v. Clutch Exchange, Inc, 701 P.2d 33, 36 (Colo. 1985).

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because they were completely dominated by the controlling shareholder/director/ president). Similarly, in Packer v. Yampol, 12 Del. J. of Corp. Law 332 (Del. Ch. Apr. 18, 1986), the court found four of five directors to be interested in a transaction with their corporation due to their "professional, financial and personal relationships" with Yampol, the corporation's chairman and chief executive officer.

What constitutes "full disclosure" by the director will be judged within the context of all the facts and circumstances of the case. De La Garza, supra, at 637. The general rule is that there must be full disclosure of all of the facts and circumstances of the transaction, the terms of the contract, and of the director's interest therein. Hudson v. American Founders Life Ins. Co., 377 P.2d 391, 397 (Colo. 1962). Accord, Smith v. Van Gorkom, 488 A.2d 858, 893 (Del. 1985); Fliegler v. Lawrence, 361 A.2d 218, 222 (Del. 1976).

By statute, Colorado and other states require full disclosure of the material facts of a director's personal interest in or relationship to a contract or transaction and as to the terms of the contract or transaction to the disinterested directors or shareholders in order for the transaction not to be voidable solely on the basis of his personal interest. Colo. Rev. Stat. § 7-5-114.5 (1986); see also Del. Code Ann. tit. 8, § 144 (1983).

Respondent has argued that this Colorado statute[8] contains the controlling definition of what constitutes a conflict of interest for purposes of this case, and governs any duty he may have to disclose and to refrain from voting. This statute is narrow in scope, however. It was enacted only to negate the early common law rule that a transaction between a director and his corporation is void or voidable solely because of the director's interest. The statute merely states the procedures or circumstances under which that doctrine may be avoided. It does

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[8] The Colorado statute provides in relevant part:

> No contract or transaction between a corporation and one or more of its directors, or between a corporation and any other corporation, partnership, association, or other organization in which one or more of its directors or officers are directors or officers or have a financial interest, shall be void or voidable solely for that reason or solely because the director or officer is present at or participates in the meeting of the board or committee thereof which authorizes, approves, or ratifies the contract or transaction or solely because his or their votes are counted for such purposes if:
>
> (a) The material facts as to his relationship or interest and as to the contract or transaction are disclosed or are known to the board of directors or the committee, and the board or committee in good faith authorizes, approves, or ratifies the contract or transaction by the affirmative vote of a majority of the disinterested directors, even though the disinterested directors are less than a quorum; or
>
> (b) The material facts as to his relationship or interest and as to the contract or transaction are disclosed or are known to the shareholders entitled to vote thereon, and the contract or transaction is specifically authorized, approved, or ratified in good faith by vote of the shareholders; or
>
> (c) The contract or transaction was fair to the corporation.

Colo. Rev. Stat. § 7-5-114.5(a) (emphasis added).

not purport to describe or encompass all rules applicable to conflicts of interest. In no event can it displace the federal standards also applicable here. See Maer, Jr. & Giacomini, The 1977 Revisions to the Colorado Corporation Code, 7 Colo. Lawyer 910, 918 (1978).

Moreover, even under such a "safe-harbor" statute, if an interested director fails to make full disclosure of all the material facts of the transaction and of his conflicting interest therein, "[t]here is no 'safe harbor' for such divided loyalties." Weinberger v. UOP, Inc., 457 A.2d at 710.

A director's fiduciary duty further requires that an interested director abstain from participating in the matter in which he has a conflicting interest and from voting on it. FSLIC v. Bass, 576 F. Supp. 848, 852 (N.D. Ill. 1983) (director of a financial institution who has a personal interest in a matter should abstain from the board deliberations on the matter and from voting on the matter). See also 12 C.F.R. § 215.4(b)(i) (FRB regulation on approval of extension of credit to bank director prohibits interested director from participating and voting on matter); 12 C.F.R. §§ 563.41(c)(3), 563.43(b)(2) (OTS regulations explicitly prohibit voting by interested director on real estate and loan transactions between the director and the institution).

In sum, the standard of conduct that applies to a director with a conflicting interest is as follows: A director of an insured depository institution who may experience a direct or indirect benefit in connection with a matter before a board of directors, has a conflict of interest and therefore would breach his fiduciary duties if he fails to disclose to the board of directors all material nonprivileged information relevant to the board's decision on the matter, or if he participates in the matter, or if he votes on it. The director must disclose: (a) the existence and the nature and extent of his conflicting interest; and (b) the facts known to the director as to the matter or transaction under consideration.[9] The director's recusal must be accompanied by disclosure of the nature and

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[9] Although the issue of the disclosure of privileged confidential information is not present in this case, there may be situations in which a director who has a conflicting interest is not able to comply fully with the disclosure requirement because of an extrinsic legally enforceable duty of confidentiality. The director's extrinsic duty may be a duty under law or professional canon, or a duty of confidentiality to another person relating to the transaction. In that circumstance, the director must disclose that he has a conflicting interest, inform the directors who vote on the matter of the nature of his duty of confidentiality, and then play no part, directly or indirectly, in their deliberations or vote. Moreover, a director could encounter the same issue with regard to any matter that comes before the board, that is, a matter in which the director has no personal interest. Under the Model Business Corporation Act the director should disclose to the other directors that he has a duty under law or professional canon, or a duty of confidentiality to another person, respecting information relating to the transaction such that the director may not make full disclosure, and withdraw from participation in the board's deliberations and action. 3 Model Business Corporation Act Annotated § 8.62(b) and Official Comment to § 8.62(b) (3d ed. 1989 Supplement).

extent of the conflicting interest and the facts known to the director as to the matter under consideration by the board.

B. The Conduct At Issue in this Case[10]

1. Walters Transactions

Between June 1986 and January 1987, the board of directors of the Association considered over $100 million in transactions involving Walters or companies in which Walters had an interest. Respondent's relationships with Walters created a significant conflict of interest, arising out of Walters' limited partnership interest in JNBE, Walters' original capital contribution of approximately half of JNBE's start-up expenses, JNBE's subsequent $100,000 indebtedness to Walters, and the credit extended to JNBE by CCNB. In addition, Respondent was personally liable as a guarantor on a portion of JNBE's debt to CCNB. Nevertheless, Respondent voted as a board member to approve those transactions. When he voted, he knew of Walters' interest in the transactions, but he failed to disclose to the other directors his business relationships with Walters or his personal and business indebtedness to CCNB, a bank controlled by Walters. He also failed to report these facts on the Association conflict of interest disclosure form provided for that purpose.

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[10] The events discussed in this section are set forth in full in the Director's Findings of Fact, attached as an Appendix to this Decision.

Respondent owed a duty of candor to explain that he had a business relationship with Walters. He failed to do so. He thereby violated his duty of candor, and deprived the other directors of the ability to evaluate his contribution to the discussions and the significance of his vote. He further owed a duty of loyalty not to vote on transactions with his business partner. He voted, and thus placed himself in a position where his interest could conflict with the Association's. He thus breached his duty of loyalty.

The Association had an internal policy on reporting potential conflicts of interest.[11] Respondent failed to report

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[11] The policy statement stated:

> It is the policy of [the Association] to require its officers and directors to devote their loyalties to the interests of the Association and to keep themselves free of influences that might conflict or appear to conflict with their representing the Association to the best of the Association's interests. . . . To avoid the development of conflict situations, each officer and director is required to submit a written statement annually [and] as soon as he/she feels that any activity, interest, or relationship of his/hers has occurred which might possibly give rise to a conflict of interest. . . . It is not the intention of [the Association] to require the officer or director to exercise independent judgment as to whether or not a specific act, interest, or relationship constitutes a conflict of interest. The officer or director should [report] any activity that might in any way be deemed to constitute such a conflict, and doubts should be resolved in favor of disclosure so that an informed judgment can thereafter be made.

his dealings with Walters on the Association disclosure form. This failure again deprived the Association of an opportunity to identify and avoid potential conflicts of interest. By violating the Association's internal policy, Respondent further breached his duty of candor.

2. <u>Good International Line of Credit Transaction</u>

In October and November 1986, the board of directors of the Association considered granting a $900,000 line of credit to Good International, Inc. ("Good International"), a company formed by Good to do business in partnership with Respondent.

Respondent formed JNB International, Inc. ("JNBI") to explore for oil and gas in Argentina. Good formed Good International to do business in Argentina with JNBI. JNBI and Good International agreed to associate as business partners and participated in a consortium that submitted a bid for government-owned oil and gas concessions in Argentina. As a condition to submitting the bid, the bidders were required to demonstrate financial strength.

In October 1986, Respondent submitted a request to the Association's management that the Association provide Good International with a $900,000 line of credit. The request included draft loan documents that Respondent's lawyers had prepared. The stated purpose of the line of credit was for use

in a presentation of Good International's financial strength to the Argentine government.

There was no disclosure of the existence of JNBI; that JNBI and Good International were partners in a consortium to do business in Argentina; that the reason Good International desired to demonstrate its financial strength to the Argentine government was to qualify the consortium to bid on oil and gas concessions in Argentina; and that JNBI anticipated receiving a financial benefit from the proposed line of credit. In November 1986, the board of directors approved the line of credit. Respondent abstained from voting.

Although Respondent's relationships with Good[12] produced significant conflicts of interest, Respondent did not disclose Good's relationship with Respondent's company, JNBI, and the fact that the proposed line of credit was to be used to qualify Respondent's enterprise to bid on oil and gas concessions in Argentina together with Good International. During this period of time, Respondent also failed to disclose this information on an Association conflict of interest disclosure form. The first time Respondent disclosed any relationship with Good on a

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[12] Good was also a limited partner in JNBE, had arranged for lines of credit for JNBE from CCNB, and had agreed to lend funds to JNBE for its operating expenses. Good actually provided over $1 million to JNBE, including funds for Respondent's salary and benefits. Good also lent Respondent personally $100,000.

disclosure form was in February 1987, some two months after the line of credit had been approved.[13]

Respondent owed a duty of candor to report that he had a substantial business interest in the proposed line of credit. He failed to do so, and thus deprived the other directors of the opportunity to evaluate the propriety and lawfulness of the transaction. Thus he violated his duty of candor.

Respondent also owed a duty of loyalty not to attempt to bring about a transaction from which he would derive a business benefit. Although Respondent abstained from voting on the line of credit, he nonetheless made efforts to secure its approval. He requested it from the Association, caused his attorneys to prepare loan documents, and presented the draft documents to the Association's management. In so doing, he breached his duty of loyalty.

3. Good Loan Modifications

In December 1986, the Association's board of directors agreed to restructure and modify certain Good loans totaling $32 million. Management and the board believed that Good was a

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[13] In the Notice of Charges, Enforcement alleged that if the line of credit had resulted in the execution of a promissory note by Good International, it would have violated the regulation prohibiting transactions with affiliated persons, 12 C.F.R. § 563.43(b). However, the record in this matter does not show execution of such a note, and a violation was not demonstrated.

troubled borrower who would not be able to meet his obligations to the Association. The loan modifications involved the release of Good's personal guaranties and collateral aggregating $28 million in return for a cash payment of $3 million. Respondent was not involved in the negotiations concerning the proposed loan modifications and he abstained from voting.

However, Respondent failed to disclose to the board, and the other directors did not know of, the existence of an earlier agreement under which Good had agreed to continue to make credit available to JNBE and to provide a promissory note of up to $5 million to fund the operations of JNBE (including Respondent's salary and benefits). Respondent also failed to disclose the probability that Respondent would be more likely to receive continued funding for his business if the Good loan modifications were approved. During this period of time, Respondent also failed to report this information on an Association conflict of interest disclosure form.

A director's duty of candor requires him to disclose the nature and extent of his conflicts of interest and all other material information relevant to a transaction under consideration by the board. Respondent had a conflict arising out of his relationships with Good and from his own potential interest in the approval of the Good loan modifications. He failed to disclose his potential interest in the board's action

or the nature and extent of his relationships with Good. Respondent also failed to share with the board the additional information that Good had recently obligated himself to continue funding JNBE and to provide up to $5 million to JNBE. Respondent was under a duty to share that information regardless of whether he had a conflicting interest. He had information concerning a borrower's financial obligations to which management and the board were not privy. He failed to disclose this information, and thus breached his fiduciary duties.

C. The Standard For Issuance of a Cease and Desist Order

At the time of Respondent's actions, section 407(e)(1) of the NHA authorized the FSLIC to issue a cease and desist order if a director of an insured institution has been, is, or is about to be engaged in an unsafe or unsound practice or is, has, or is about to violate a law, rule, or regulation. 12 U.S.C. § 1730(e)(1).[14] The history of the statute shows that Congress carefully considered the phrase "unsafe or unsound." Because the term "unsafe or unsound practice" was undefined in the statute, the House requested the Chairman of the FHLBB, John Horne, to provide guidance on the subject. The concept was explained by Chairman Horne as follows:

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[14] FIRREA repealed section 407(e) of the NHA, but the grounds for issuance of a cease and desist order set forth therein still govern actionable conduct that occurred prior to FIRREA. *See* section 401(f) of FIRREA. Post-FIRREA, the authority of the OTS to issue a cease and desist order is derived from section 8(b) of the FDIA.

> Like many other generic terms widely used in the law, such as "fraud," "negligence," "probable cause," or "good faith," the term "unsafe or unsound practices" has a central meaning which can and must be applied to constantly changing factual circumstances. Generally speaking, an "unsafe or unsound practice" embraces any action, or lack of action, which is contrary to generally accepted standards of prudent operation, the possible consequences of which, if continued, would be abnormal risk or loss or damage to an institution, its shareholders, or the agencies administering the insurance funds.

Financial Institutions Supervisory and Insurance Act of 1966: Hearings on S. 3158 and S. 3695 Before the House Committee on Banking and Currency, 89th Cong., 2d Sess. 49-50 (memorandum submitted by John Horne) (emphasis added; citations omitted).

This definition has gained wide acceptance among the banking agencies and the courts.[15] Under it, the regulatory agencies have broad authority to identify unsafe or unsound practices.[16] The courts have recognized that the very purpose of using so

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[15] See, e.g., Van Dyke v. Board of Governors of the Federal Reserve System, 876 F.2d 1377, 1380 (8th Cir. 1989); Matter of Rodriques, FHLBB Res. No. 88-1564 at 49 (OTS Final Decision issued pursuant to OTS Res. No. 89-447, dated December 5, 1989); In the Matter of Anonymous, FDIC Docket No. FDIC 85-215e (7-17-86), reprinted in 1 FDIC Enforcement Decisions and Orders ¶ 5069.14 (1986); In the Matter of Anonymous, FDIC Docket No. FDIC 84-58e (1-25-85), reprinted in 1 FDIC Enforcement Decisions and Orders ¶ 5042.9 (1985); First Nat'l Bank of Lamarque v. Smith, 610 F.2d 1258, 1265 (5th Cir. 1980); First Nat'l Bank of Eden v. Dept. of the Treasury, 568 F.2d 610, 611 n.2 (8th Cir. 1978).

[16] In administrative proceedings, what is unsafe or unsound may properly be established by the expert testimony of bank or thrift examiners. Sunshine State Bank v. FDIC, 783 F.2d 1580, 1582-83 (11th Cir. 1986); First Nat'l Bank of Eden v. Dept. of the Treasury, 568 F.2d at 611.

generic a term was to permit the regulatory agencies the flexibility necessary to respond to new or different situations to protect the public and the Nation's federal deposit insurance funds. In re Franklin Nat'l Bank Securities Litigation, 478 F. Supp. 210, 218 (E.D.N.Y. 1979). As the Fifth Circuit has stated:

> The phrase "unsafe or unsound banking practice" is widely used in the regulatory statutes and in case law, and one of the purposes of the banking acts is clearly to commit the progressive definition and eradication of such practices to the expertise of the appropriate regulatory agencies.

Groos Nat'l Bank v. Comptroller of the Currency, 573 F.2d 889, 897 (5th Cir. 1978). See Independent Bankers Ass'n v. Heimann, 613 F.2d 1164, 1168-69 (D.C. Cir. 1979), cert. denied, 449 U.S. 823 (1980) (discretionary authority to define and eliminate "unsafe and unsound" conduct is to be liberally construed).

Consistent with the definition of unsafe or unsound practice in the legislative history, the case law holds that the appropriate standard for the issuance of a cease and desist order is: (1) whether the conduct is contrary to generally accepted standards of prudent operation of a financial institution, (2) the possible consequence of which, if continued, may be abnormal risk, or loss, or damage to an institution, its shareholders, or the insurance fund. See First Nat'l Bank of Eden v. Dept. of the

Treasury, 568 F.2d at 611 n.2.[17]

Respondent's conduct constitutes unsafe or unsound practices under the standards recognized by Congress and the courts.

First, in each of the situations described above, Respondent breached his fiduciary duties by failing to disclose a conflict of interest. Thus he obviously acted in a manner contrary to generally established standards of prudent operation of a financial institution. Respondent's voting on the Walters transaction was also contrary to such standards.

Second, this conduct exposed the Association to the possibility of abnormal risk because it impaired the decision-making process of the board. The consequences of a director's failure to disclose that he, or his primary business, would benefit from matters put to the board for decision can be substantial. To omit to disclose such information deprives the

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[17] Respondent has asserted that a third element is required: that the conduct have "a reasonably direct effect on an association's financial soundness." This additional element was suggested -- 15 years after the passage of the Financial Institutions Reform Act -- by the Fifth Circuit in Gulf Federal Savings & Loan Ass'n v. FHLBB, 651 F.2d 259, 264 (5th Cir. 1981), cert. denied, 458 U.S. 1121 (1982). A requirement of such a showing is fundamentally inconsistent with the purpose of a cease and desist order, which is to try to stop harm to an institution before it occurs. Saratoga Savings & Loan Ass'n v. FHLBB, 879 F.2d 689, 693 (9th Cir. 1989). The Director accordingly rejects Respondent's argument that such a third element is required to establish that conduct is unsafe or unsound.

board of the opportunity to consider all pertinent facts when deciding a matter before it. The resulting uninformed decision-making exposes an insured depository institution to abnormal risk.

Furthermore, a director's failure to abstain from voting on an institution's transactions with his business partner exposes the institution to abnormal risk because of the impairment of the director's independent business judgment. When the interests of the institution and the business partner do not coincide (as is the case when the institution is a lender and the business partner is a borrower), the director may resolve doubts about the wisdom of corporate action in a manner favorable to his business partner. The director may be unable to discern impartially the merits of a transaction that would benefit his business partner. Such lack of impartiality poses an abnormal risk to insured depository institutions. Prevention of such risk and its possible adverse consequences is a fundamental objective of the cease and desist process. Accordingly, the Director concludes that grounds exist for the issuance of a cease and desist order against Respondent.

D. Other Issues of Law and Procedure

The remaining issues fall into the following general categories: the independence of the trier-of-fact; the remedy to be imposed; and the ALJ's rulings on various motions.

1. Independence of Judgment

Respondent maintains that the ALJ essentially adopted Enforcement's proposed findings of fact and conclusions of law wholesale without reviewing the record and exercising his own judgment. The Director's review of the ALJ's Recommended Decision, however, shows that the ALJ did not uncritically adopt the agency's proposed findings and conclusions without further consideration or elaboration. The record shows that the ALJ reviewed the record and exercised his own judgment in formulating his findings and reaching his conclusions.[18] The ALJ did not adopt either party's proposed findings and conclusions verbatim and incorporate them in his Recommended Decision. Accordingly, the Director rejects Respondent's exception that the ALJ failed to exercise independent judgment in reaching his Recommended Decision.

2. The Parties' Exceptions to the Recommended Remedy

a. Availability of the Cease and Desist Order

Respondent contends that a cease and desist order is not appropriate in this case because Respondent no longer serves as a

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[18] In any event, while appellate tribunals uniformly criticize a trier-of-fact's wholesale adoption of a party's findings or brief, such a decision will not be overturned unless it is clearly erroneous. See Anderson v. Bessemer City, 470 U.S. 564, 572 (1984); DiLeo v. Ernst & Young, 901 F.2d 624, 626 (7th Cir.), cert. denied, 111 S.Ct. 347 (1990); Walton v. United Consumers Club, Inc., 786 F.2d 303, 314 (7th Cir. 1986).

director of the Association and the Association itself no longer exists. According to Respondent, cease and desist proceedings are preventive actions to correct unsafe or unsound practices "affecting the continued viability of an ongoing federally-insured institution" and, as such, may not be based on past acts unless a reasonable likelihood of recurrence exists. Brief in Support of Bush's Exceptions to the ALJ's Decision at 6-8, citing Gulf Federal Savings & Loan Ass'n v. FHLBB, 651 F.2d 259, 263 (5th Cir. 1981), cert. denied, 458 U.S. 1121 (1982); First National Bank of Bellaire v. Comptroller of the Currency, 697 F.2d 674, 681 (5th Cir. 1983). Respondent further asserts that a cease and desist order, like an injunction, is not warranted because the ALJ did not find that Respondent acted in bad faith. See Aaron v. SEC, 446 U.S. 680 (1980); SEC v. Haswell, 654 F.2d 698 (10th Cir. 1981).

These arguments are without merit. Section 8(i) of the FDIA, as amended by section 905(a) of FIRREA, expressly authorizes the OTS to bring cease and desist actions even though the institution-affiliated party charged may have resigned from the institution or the institution may have closed. 103 Stat. at 459 (to be codified at 12 U.S.C. § 1818(i)(3)). See also H.R. Conf. Rep. No. 1278, 101st Cong., 1st Sess. 440 (1989). Congress explicitly provided that such authority is retroactive, subject to a six-year statute of limitations. Id. By its terms, therefore, the FDIA provides for cease and desist orders directed

at past misconduct regardless of the status of the respondent or the institution.

Respondent also argues, in essence, that his resignation and the closing of the Association foreclose a finding that a reasonable likelihood of recurrence exists. Since Congress has expressly authorized cease and desist actions against officers and directors who have resigned or separated from closed institutions, Congress could not have intended that those events would preclude issuance of a cease and desist order. Moreover, as a practical matter, the possibility exists that at some time in the future, Respondent could serve again as a director of an insured depository institution.

With regard to his assertion of a good faith defense against a cease and desist order, Respondent relies primarily on cases arising under the federal securities laws. See Aaron v. SEC, 446 U.S. 680; SEC v. Haswell, 654 F.2d 698. Respondent's reliance on this argument and the associated case law is misplaced. The courts have required a showing of scienter to support issuance of injunctions against violations of certain antifraud provisions of the securities laws. Aaron v. SEC, 446 U.S. at 701-702; SEC v. Haswell, 654 F.2d at 699.

Neither section 407(e) of the NHA nor section 8(b) of the FDIA contains a scienter requirement. 12 U.S.C. § 1730(e);

FIRREA § 902(a), 103 Stat. at 446-48 (to be codified at 12 U.S.C. § 1818(b)). The Director does not interpret the OTS's cease and desist authority to require a showing of scienter prior to the issuance of such orders, and, on that basis, he rejects Respondent's argument that good faith, even if demonstrated, would preclude the issuance of a cease and desist order under these circumstances.

b. Exceptions to the Recommended Order

The ALJ recommended that the Director issue an order requiring Respondent to cease and desist from: any acts, omissions, or practices involving conflicts of interest as defined in 12 C.F.R. § 571.7; any acts, omissions, or practices which constitute a breach of fiduciary duty; and any unsafe or unsound practice as an institution-affiliated party. In addition, the ALJ suggested that Respondent be required to perform certain affirmative actions upon joining the board of any federally insured depository institution or holding company thereof.

Respondent submitted exceptions to each paragraph of the ALJ's recommended order to cease and desist. Generally, Respondent contends that the recommended order is both unduly vague and overly broad.

The Director rejects Respondent's argument that ordering compliance with section 571.7 is impermissible because its provisions are unconstitutionally vague. In fact, both the language of the regulation and the common law that has arisen regarding conflicts of interest have established well-recognized standards of behavior for officers and directors of financial institutions. The Director has found that Respondent engaged in activities inconsistent with the standard articulated by section 571.7, which embodies well-established principles of federal and common law. It is, therefore, appropriate to order Respondent in the future to conform his behavior to section 571.7, the common law, and the standards discussed in this Decision.

Contrary to Respondent's exceptions to paragraphs 4(a) and (b) of the recommended order, it is also appropriate, in view of the Director's conclusions regarding the transactions at issue in this case, to order Respondent to seek legal advice in connection with any future service as a director and to abstain from voting or participating in those matters where he has a personal interest and may experience a direct or indirect benefit. Similarly, the Director's conclusions concerning these transactions, in large part affirming the ALJ's findings, demonstrate the necessity of ordering Respondent to refrain from future breaches of his fiduciary duties and unsafe or unsound practices, as discussed in this Decision, despite his exceptions to paragraphs 2 and 3 of the ALJ's recommended order.

In addition, with regard to Respondent's objections to paragraphs 4(c) and (d) of the recommended order concerning the extent of disclosure to be required, the Director concludes that those paragraphs were intended only to require compliance with fiduciary duties of directors, as discussed in this Decision.

Finally, the Director has reviewed paragraph 5 of the recommended order, in which the ALJ ordered Respondent to cease and desist from any violations of various statutory and regulatory provisions governing transactions with affiliates, as well as section 571.7. In light of the Director's findings of fact and conclusions of law regarding Respondent's activities contained in this Decision, the Director declines to accept the ALJ's recommendation, except with regard to section 571.7. See paragraph 2(e) of the attached Order.

Enforcement in turn seeks to enhance the recommended order to require that, prior to serving as an institution-affiliated party in the future, Respondent demonstrates the ability to recognize and react to actual, potential, and apparent conflicts of interest. In its exception, Enforcement suggests that Respondent be prohibited from future service until such ability is shown by his actions, education, or similar means. The Director believes, however, that the attached order to cease and desist is adequate to prevent future conflict of interest abuses.

by Respondent without the additional conditions sought by Enforcement.

3. Exceptions to the ALJ's Rulings on Motions for Summary Disposition and to Amend the Notice of Charges

Respondent's exceptions to the ALJ's denial of his motion for summary disposition and the ALJ's granting of Enforcement's motion to amend the notice of charges merely restate his arguments before the administrative law judge. These exceptions are also without merit. The ALJ has broad discretion to allow either party to amend its pleadings throughout the administrative proceedings, and the Director finds no evidence to indicate that the ALJ abused his discretion in this instance. 12 C.F.R. § 509.15.[19]

Respondent also renews his objection to the ALJ's denial of his motion for summary disposition based on Respondent's assertion that a cease and desist order is no longer available following his resignation and the closing of the Association.

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[19] Enforcement was allowed to amend its Notice of Charges and Hearing merely to conform the pleading to the evidence and to clarify that the charges involved both the breach of fiduciary duties and unsafe or unsound practices. The ALJ expressly concluded that the acts that formed the basis for the Notice remained unchanged and that Respondent had actual notice of Enforcement's intention to pursue the issue of unsafe or unsound practices throughout these proceedings. The ALJ also gave Respondent the opportunity to present additional evidence in response to the amended pleading. Order (Oct. 5, 1990) (granting OTS's Motion to Amend Notice of Charges).

The Director upholds the ALJ's denial of Respondent's motion for summary disposition because, as previously discussed, FIRREA amended this agency's cease and desist authority to allow such proceedings against officers and directors who have resigned or institutions that have closed. 103 Stat. at 459 (to be codified at 12 U.S.C. § 1818(i)).