FEDERAL DEPOSIT INSURANCE CORPORATION
WASHINGTON, D.C.

In the Matter of	)
DOUGLAS V. CONOVER, individually, and as an institution-affiliated party of	) DECISION AND ORDER TO) PROHIBIT FROM FURTHER) PARTICIPATION AND ASSESSMENT) OF CIVIL MONEY PENALTIES
FIRST STATE BANK, CRANFORD, NEW JERSEY	) FDIC-13-214e) FDIC-13-217k
(In Receivership)	)

I. INTRODUCTION

This matter is before the Board of Directors ("Board") of the Federal Deposit Insurance Corporation ("FDIC") following the issuance on April 13, 2016, of a Recommended Decision ("Recommended Decision" or "R.D.") by Administrative Law Judge C. Richard Miserendino ("ALJ"). The ALJ recommended that the respondent, Douglas V. Conover ("Respondent"), be subject to an order of prohibition pursuant to section 8(e) of the Federal Deposit Insurance Act ("FDI Act"), 12 U.S.C. § 1818(e), and be assessed a civil money penalty ("CMP") pursuant to section 8(i) of the FDI Act, 12 U.S.C. § 1818(i). For the reasons discussed following, the Board adopts and affirms the Recommended Decision, to the extent it is consistent with this Decision, and issues against Respondent an Order of Prohibition and Order to Pay a CMP in the amount of $25,000.

II. PROCEDURAL HISTORY

The FDIC initiated this action on July 12, 2013, when it issued against Respondent,

individually, and as an institution-affiliated party of First State Bank, Cranford, New Jersey (the "Bank"),[1] a Notice of Intention to Remove from Office and to Prohibit from Further Participation, Assessment of Civil Money Penalty, Findings of Fact and Conclusions of Law, Order to Pay, and Notice of Hearing ("Notice"). During the pertinent time period, Respondent was the Executive Vice President and Chief Lending Officer of the Bank. (R.D. at 1.)[2] The Notice charged Respondent with engaging and participating in regulatory violations, unsafe and unsound banking practices, and breaches of fiduciary duty. (Notice ¶¶ 51-52.) The Notice also alleged that Respondent acted with personal dishonesty and demonstrated willful or continuing disregard for the safety and soundness of the Bank. (*Id.* ¶ 54.) The Notice included an Order to Pay a CMP in the amount of $25,000. (*Id.* ¶ 58; R.D. at 2.)

Among other things, the Notice alleged that Respondent violated Regulation O, 12 U.S.C. § 375a & 12 C.F.R. Part 215, by approving loans to affiliates of a bank insider without obtaining the consent of the Bank's full board of directors. (Notice ¶¶ 31, 45.) The Notice further alleged that Respondent engaged in breaches of fiduciary duty and unsafe and unsound banking practices by approving loans to a nominee borrower on behalf of a bank insider without adequate assurance of repayment. (*Id.* ¶¶ 48-50.) The Notice further alleged that Respondent was aware that the loan was for the benefit of a bank insider but did not inform the Bank's board of directors. (*Id.*)

On July 22, 2013, Respondent filed a timely Answer to the Notice, denying the material

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[1] On October 14, 2011, the New Jersey Department of Banking and Insurance closed the Bank and appointed the FDIC as receiver. (R.D. at 3.)

[2] Citations to the factual findings of the Recommended Decision encompass the record citations on the cited pages of that decision, and those record citations accordingly are not repeated here. The transcript of the January 2013 hearing before the ALJ is cited as "Tr." The joint exhibits at that hearing are cited as "Jt. Ex.," the FDIC's exhibits are cited as "FDIC Ex.," and Respondent's exhibits are cited as "Resp. Ex."

allegations therein. Respondent filed an Amended Answer on August 8, 2014. (R.D. at 2.) Following extensive discovery, a two-day hearing on the merits of the charges was held in Cherry Hill, New Jersey, in November 2014. At the hearing, the ALJ received sworn testimony from Respondent as well as from two witnesses called by FDIC Enforcement Counsel ("Enforcement Counsel") and one witness called by Respondent.

On April 13, 2016, the ALJ issued a 57-page Recommended Decision recommending that Respondent be prohibited from participation in the banking industry and be ordered to pay a CMP as assessed in the Notice, though the ALJ did find that Respondent did not violate Regulation O when he caused another bank to issue letters of credit. Both Respondent and Enforcement Counsel timely filed exceptions. On September 20, 2016, pursuant to 12 C.F.R. § 308.40(c)(2), the FDIC Assistant Executive Secretary transmitted the record in the case to the Board for final decision.

III. BACKGROUND

Because the ALJ provided a lengthy, detailed, and well-reasoned opinion with extensive citations to the record in support of his conclusions, the Board finds it unnecessary to reiterate in full the contents of the Recommended Decision. The following discussion, however, highlights certain aspects of Respondent's misconduct as alleged in the Notice, corroborated by supporting testimonial and documentary evidence, and recounted in the Facts section of the Recommended Decision.

A. Regulation O

Regulation O addresses the circumstances under which credit may be extended to bank "insiders," defined as executive officers, directors, principal shareholders, and any related interests of those persons. 12 C.F.R. § 215.2(h). Credit is deemed extended to bank insiders if a

loan or line of credit is extended to a bank insider (or related interest), such that the proceeds are transferred to the insider or the insider derives a "tangible economic benefit" from the loan. *Id.* § 215.3(f).

Under Regulation O, credit may be extended to bank insiders only "on substantially the same terms . . . as, and following credit underwriting procedures that are not less stringent than, those prevailing at the time" for non-insiders. *Id.* § 215.4(a)(1)(i). Furthermore, the extension of credit cannot "involve more than the normal risk of repayment or present other unfavorable features," *id.* § 215.4(a)(1)(ii), and the aggregate extension of credit to any one insider and his related interest may not exceed $500,000 without advance approval by a majority of the "entire board of directors of the bank." *Id.* § 215.4(b)(1)(i).

Regulation O has specific requirements governing the extensions of credit to executive officers and their related interests. Extensions of credit to an executive officer other than for mortgages on a principal residence or for education may not exceed an aggregate of $100,000. *Id.* § 215.5(c)(4). Furthermore, all extensions of credit to executive officers must be reported to the board of directors (whether or not they exceed the thresholds), must be accompanied by detailed financial statements of the executive officer, and must be subject to the condition that the bank can require immediate payment from the executive officer if the officer becomes indebted to any other bank in an amount greater than the $100,000 threshold. *Id.* § 215.5(d)(4).

Regulation O's requirements were mirrored in the Bank's Loan Policy. (Jt. Ex. 2 at 47.) The Loan Policy further provided that loans to bank insiders or related interests "must be approved by the *full* Board," and not simply by the board's Executive Loan Committee. (Jt. Ex. 2 at 17.)

B. First State Bank

The Bank opened on January 18, 2006. (Jt. Ex. 40 ¶ 1.) From that time until September 2009, Respondent was the Executive Vice President and Chief Lending Officer of the Bank. (R.D. at 3, 17 n.21.) Respondent had served for over 30 years in the banking industry, including multiple stints as Chief Lending Officer at various small banks. (R.D. at 3.) Respondent's duties included soliciting new loan business, initiating the loan approval process, and supervision of lending officers, underwriters, and loan administrators. (R.D. at 3.)

Because the Bank was a new entity, it lacked the credit quality in 2007 and 2008 to issue letters of credit. (R.D. at 35.)[3] Such banks typically enlist the services of a correspondent bank to issue the letter of credit; the letter of credit is supported by a promissory note for a line of credit, executed by the borrower and the new bank. (R.D. at 35.) Atlantic Credit Banker's Bank ("ACBB") was First State Bank's correspondent bank. (Jt. Ex. 40 ¶ 9.)

At all relevant times, Joseph Natale was the Chairman of the board of directors and Chief Executive Officer of the Bank. (Jt. Ex. 40 ¶ 8.) Natale's business interests included a real estate development company, JDN Properties at Florham Park LLC ("JDN FloPark"). (Tr. at 29.)

C. $500,000 Extension of Credit to [redacted]

On August 8, 2007, a New Jersey court issued a writ of attachment in the amount of $500,000 against JDN FloPark to secure a judgment for damages arising out of a construction defect claim. (R.D. at 5.) The court attached the proceeds of the sale of three properties "until

[3] A letter of credit is an institution's promise to pay a specific sum on behalf of a certain beneficiary, typically to the beneficiary's creditors, upon demand (rather than the beneficiary putting funds in escrow). Letters of credit are often used as appeal bonds in litigation, furnishing proof that a defendant appealing a judgment will pay the judgment if the appeal is unsuccessful. They are often supported by promissory notes establishing *lines* of credit for the letter's beneficiary. Under those arrangements, draws on the letter of credit will be charged to the line of credit, and the beneficiary must repay the bank under the terms set forth in the promissory notes, just as if the beneficiary had drawn on bank funds directly. *See, e.g.*, *FDIC v. Philadelphia Gear Corp.*, 476 U.S. 426, 428 (1983); *Kaysville City v. FDIC*, 557 F. App'x 719, 722-23 (10th Cir. 2014).

judgment is paid in full or further order of this Court." (Jt. Ex. 3 at 2.) The defendants in the lawsuit in question included [redacted] one of JDN FloPark's construction contractors, though the writ of attachment was specifically directed at properties owned by JDN FloPark. (R.D. at 5; Jt. Ex. 3 at 2; Tr. at 447.) Shortly thereafter, Natale directed Respondent to contact [redacted] daughter, about a $500,000 letter of credit. (R.D. at 5.) [redacted] was out of the country at that time. (R.D. at 6.) On August 29, 2007, Respondent contacted an employee at another company owned by Natale, First United Mortgage, stating, "Joe asked me to send a list of what we need to provide a Letter of Credit for the daughter of [redacted] (R.D. at 5-6.) Respondent enumerated four items, including "[a]n explanation of what the $500,000 letter of credit is for [and] who the beneficiary is," and further noted that "[i]f any of this is not clear or Joe would like me to speak directly with Mr. [redacted] please have them call me." (R.D. at 6.) Respondent went on to note that "Joe would like to get this approved at next Thursday's loan committee meeting." (R.D. at 6.) The First United employee told Respondent that his e-mail had been forwarded to [redacted] and [redacted] (R.D. at 6.) Subsequently, [redacted] mother sent Respondent [redacted] financial information, stating that "Joe's office is preparing the letter of explanation and Joe's lawyer, Keith McKenna, is preparing the LOC." (R.D. at 6.)

On September 13, 2007, the Bank's Executive Loan Committee approved a $500,000 letter of credit to [redacted] supported by a $500,000 credit line. (R.D. at 6-7.) Respondent presented the proposal. (R.D. at 6.) The Loan Approval Document supporting the proposal asserted that the letter of credit was intended for the benefit of [redacted] pertaining to structural damage to a customer's property, without mentioning any benefit to Natale:

> [T]he customer subsequently took the matter to court, which decided that Mr. [redacted] needed to complete the repairs which an engineer estimated to be approximately $500,000. . . . The court allowed Mr. [redacted] to undergo the repairs but required a letter of credit be issued for $500,000 which could be drawn

on in the event the repairs are not handled as agreed.

(Jt. Ex. 10 at 2.) The line of credit was to expire in one year, with interest payable monthly and the principal due at maturity, and was secured by a second mortgage on a vacation property owned by [redacted] (R.D. at 6; Jt. Ex. 10 at 2.) The property had been valued at $2.4 million, and was already encumbered by a first mortgage in the amount of $1.5 million. (Jt. Ex. 10 at 2.) Respondent did not present the [redacted] letter of credit application to the full board.

The Bank issued an irrevocable letter of credit on September 25, 2007. (Jt. Ex. 13.) It was not directed to, and did not mention, [redacted] (*Id.*) Rather, it was directed to "Mark L. Breitman, Attorney at Law," identifying Breitman as the "Beneficiary," and stated that "a final non-appealable judgment has been entered in the matter entitled 'Dr. [redacted] et al vs. JDN Properties at Florham Park, LLC, et al.' . . . in favor of the plaintiff, Dr. [redacted] et al." (*Id.*) Breitman was an attorney for JDN FloPark, and was also a member of the Bank's Executive Loan Committee. (Jt. Ex. 40 ¶ 19; Tr. at 51, 117.) The letter of credit further provided that it would remain in effect for one year and would be automatically renewed for subsequent years unless revoked by the Bank. (Jt. Ex. 13.)

D. $250,000 ACBB Letter of Credit to JDN FloPark

On November 23, 2007, the New Jersey court rejected the [redacted] letter of credit, and increased the required amount. (R.D. at 9.) It directed JDN FloPark to "obtain a Letter of Credit in the amount of $750,000 from an *independent bank* approved of by Plaintiffs' counsel." (R.D. at 9.) (emphasis added) Notwithstanding that direction, on January 10, 2008, Respondent submitted a memorandum to the Bank's Executive Loan Committee, seeking to increase the [redacted] letter of credit to $750,000 in light of "recent court proceedings." (R.D. at 9.) The Committee approved the request. (R.D. at 9.) Respondent did not present this request to the full

board. Notably, Respondent did not increase [redacted] line of credit by a corresponding amount, and [redacted] does not appear to have been notified of the change, let alone requested it. (R.D. at 9.)

The increased [redacted] letter of credit was not satisfactory (and does not appear to have been executed), however. Because, contrary to the court's instructions, it was not issued by an independent bank, the court refused to accept it. (R.D. at 9; Tr. at 78-80, 146-47, 623-24.) Respondent sought the assistance of ACBB as a correspondent bank. (R.D. at 10.) At Respondent's request, on March 4, 2008, ACBB agreed to issue a $250,000 letter of credit (not $750,000, despite the court's instructions), supported by a $250,000 line of credit issued by the Bank. (R.D. at 10-11.) The line of credit, unlike the [redacted] line of credit discussed above, was unsecured. (R.D. at 10.) Respondent agreed that the Bank would pledge $250,000 in securities to ACBB, and that, if the letter of credit were called, ACBB was authorized to draw funds from the Bank's demand deposit account at ACBB or liquidate the securities—in either event, transferring the burden from ACBB to the Bank. (R.D. at 10-11.) Thus, ACBB assumed no risk in issuing the letter of credit. (R.D. at 11.) The line of credit was issued by the Bank on March 5, 2008, and it expired on March 5, 2009. (Jt. Ex. 18 at 9.)

Notably, ACBB issued the $250,000 letter of credit not for the benefit of [redacted] but rather for JDN FloPark. (R.D. at 10, 12.) Respondent submitted a request to the Bank's board of directors (not to the Executive Loan Committee) for approval of a $250,000 line of credit for the benefit of JDN FloPark, expressly acknowledging the link between the $250,000 request for JDN FloPark (Natale's company) and the existing $500,000 letter of credit, nominally for [redacted] that had already been approved:

> In 2007, the Bank approved a similar facility to [redacted] ($500,000), daughter of [redacted] who was engaged to construct the properties in the

> JDN development. . . . Subsequently, the amount requested has been increased to $750,000, resulting in our seeking approval for the $250,000 balance.

(Jt. Ex. 17 at 2.) Respondent did not question the appropriateness of the $500,000 letter of credit at that time, however, or raise any concerns with the board about that letter of credit, or how it was obtained. (R.D. at 10.) Furthermore, the Loan Approval Document submitted to the board described the line of credit to JDN FloPark as a 100 percent "participation" with ACBB, even though, as noted above, ACBB bore none of the risk. (Jt. Ex. 17 at 1.) The Loan Approval Document did not disclose that the Bank would pledge $250,000 in securities to ACBB or authorize the debiting of its demand deposit account. (Jt. Ex. 17.)

On March 10, 2008, ACBB issued the $250,000 letter of credit to Breitman. (Jt. Ex. 18 at 15.) The letter of credit was directed to Breitman as "Beneficiary" and identified JDN FloPark as "our client" and "Principal." (Jt. Ex. 18 at 15.) The letter was to expire after one year, and, unlike the [redacted] letter of credit, contained no automatic renewal provision. (Jt. Ex. 18 at 15.) Accompanying the letter was a loan participation agreement, signed by Respondent, stating that ACBB was purchasing the Bank's percentage of the loan, though ACBB paid no money to the Bank at that time. (R.D. at 12.) Respondent authorized ACBB to debit the Bank's demand deposit account in the event of a draw on the letter of credit, and ACBB also received a pledge of Bank securities with a value of $250,000 as collateral. (R.D. at 12; Jt. Ex. 18 at 18.) The agreement contained an indemnification clause under which the Bank agreed to indemnify ACBB for any losses suffered as a result of the Bank's breaches of its obligations. (R.D. at 12-13.)

E. Replacement of the Bank's $500,000 [redacted] Letter of Credit with a $500,000 [redacted] Letter of Credit Issued By ACBB

In June 2008, the Bank approached ACBB, seeking to replace the $500,000 [redacted] letter

of credit issued by the Bank with a similar letter issued by ACBB. (R.D. at 13.) The New Jersey court had deemed the existing letter unacceptable because the Bank did not have sufficient credit quality. (Tr. at 79-80.) ACBB therefore issued a $500,000 letter of credit for the benefit of [redacted] similar to the $250,000 letter of credit issued for the benefit of JDN FloPark, on July 15, 2008. (Jt. Ex. 23 at 87.) As with the earlier ACBB letter of credit for JDN FloPark, the $500,000 ACBB letter of credit for [redacted] was supported by a $500,000 line of credit issued by the Bank, and the Bank authorized the debiting of its demand deposit account, and pledged $500,000 in securities to ACBB, to eliminate any risk to ACBB. (R.D. at 14-15; Jt. Ex. 23 at 65.) As with the either ACBB letter of credit, the $500,000 letter was directed to Breitman as "Beneficiary," though it identified [redacted] as "our client" and "Principal." (Jt. Ex. 23 at 87.) Unlike the earlier ACBB letter of credit, however, the $500,000 letter of credit provided that it would automatically renew, at one-year intervals, unless canceled by ACBB. (Jt. Ex. 23 at 87.) The internal ACBB memo noted that the letter of credit was intended to support JDN FloPark's obligations in the litigation, stating that the court had ordered JDN FloPark to repair certain property and "required a letter of credit be issued for $500,000 which could be drawn upon if repairs were not handled as agreed," and describing the March 2008 $250,000 ACBB line of credit to JDN FloPark as addressing the same obligation. (Jt. Ex. 23 at 4.) The internal ACBB memo also noted that the Bank's original $500,000 letter of credit to [redacted] would be returned once ACBB's $500,000 letter of credit was issued. (Jt. Ex. 23 at 4.)

On July 15, 2008, Respondent signed a loan participation agreement, similar to the earlier agreement, stating that ACBB was purchasing the Bank's percentage in the loan and indemnifying ACBB for any losses sustained as a result of the Bank's breaches. (R.D. at 14-15.) Respondent also authorized the debiting of the Bank's demand deposit account at ACBB, and

signed a pledge of $500,000 in the Bank's securities to ACBB as collateral. (R.D. at 15; Jt. Ex. 23 at 84.) There is no record of any presentation of these commitments to the Committee or the board by Respondent, or anyone else.

No new line of credit and promissory note was executed by [redacted] or the Bank in connection with the issuance of the ACBB letter of credit, however. (R.D. at 16.) The existing line of credit, originally executed on September 25, 2007, remained the sole repayment commitment supporting the ACBB letter of credit. (R.D. at 16.) The promissory note reflecting that line of credit expired on September 25, 2008, and it was not renewed, despite ACBB's requests. (R.D. at 16-17.) Once the note expired, therefore, ACBB had no line of credit in [redacted] name to debit should the letter of credit be called, and [redacted] had no obligation to repay any indebtedness resulting from such a call. (R.D. at 16.) The $500,000 letter of credit, however, remained in force and was not canceled. (R.D. at 17; Tr. at 98-99.)

[redacted] subsequently sued ACBB, alleging that the $500,000 letter of credit was issued without her authorization. (Jt. Ex. 36; Tr. at 93.)

E. Expiration of the $250,000 ACBB Letter of Credit

On March 5, 2009, ACBB's $250,000 letter of credit for the benefit of JDN FloPark, and the Bank's $250,000 line of credit, both expired. (R.D. at 15; Jt. Ex. 18 at 9.) Neither was renewed prior to that date. (R.D. at 15.) On April 9, 2009, Respondent contacted ACBB regarding the renewal of the letter of credit, but after ACBB requested information about the status of the project, the Bank's renewal of the line of credit, and financial information about JDN FloPark, Respondent abandoned the effort to get a renewed $250,000 letter of credit. (R.D. at 15-16.) Respondent left the Bank in September 2009. (Tr. at 628.)

F. Call of the $250,000 ACBB Letter of Credit

On September 30, 2010, ACBB converted the $500,000 in securities that the Bank had pledged in support of the [redacted] letter of credit to a $500,000 certificate of deposit—effectively turning those securities into cash. (R.D. at 17.)

On February 25, 2011, the $500,000 ACBB letter of credit was called, and ACBB paid the plaintiff in the New Jersey litigation $500,000 in accordance with the terms of that letter. (R.D. at 17.) ACBB subsequently liquidated the $500,000 certificate of deposit, and debited the Bank's demand deposit account at ACBB in the amount of $87,262.73 to cover attorney's fees and expenses incurred by ACBB in connection with the New Jersey litigation, as well as separate litigation, referenced above, with [redacted] regarding the validity of the ACBB letter of credit. (R.D. at 17.) The Bank therefore sustained a $587,262.73 loss on the $500,000 [redacted] letter of credit, and efforts to foreclose on the [redacted] mortgage were unsuccessful. (Resp. Exs. 5, 6.)

IV. ANALYSIS

A. A Prohibition is Warranted.

As noted in the Recommended Decision, Enforcement Counsel—to carry their burden in a prohibition action—must show that Respondent engaged in prohibited conduct (misconduct), the effect of which was to cause the Bank to suffer financial loss or damage, to prejudice or potentially prejudice the Bank's depositors, or to provide financial gain or other benefit to the Respondent (effects). Enforcement Counsel must also demonstrate that such misconduct evidences personal dishonesty or a willful or continuing disregard for the safety and soundness of the Bank (culpability). 12 U.S.C. § 1818(e)(1); R.D. at 20; *see In the Matter of Ramon M. Candelaria*, 1997 WL 211341, *3 (FDIC Mar. 11, 1997), *aff'd*, 1998 WL 43167 (10th Cir. Feb. 3, 1998); *In the Matter of James L. Leuthe*, 1998 WL 438323, *11 (FDIC June 26, 1998), *aff'd*, 194 F.3d 174 (D.C. Cir. 1999). As discussed below, the Board finds that the activities of

Respondent during the pertinent time period satisfy the three standards necessary to impose a prohibition.

Misconduct

Misconduct under section 8(e) encompasses violations of governing laws and regulations, along with participation in activity deemed to be an unsafe and unsound banking practice or in breach of a party's fiduciary duty. 12 U.S.C. § 1818(e)(1)(A). The record clearly establishes Respondent's regulatory violations, unsafe and unsound practices and breaches of fiduciary duty.

1. Regulation O Violations

As set forth above, Regulation O prohibits the extension of credit to a bank insider or a bank insider's related interests without the consent of the full board of directors. Conferring a "tangible economic benefit" on a bank insider or the insider's interests implicates Regulation O. 12 C.F.R. § 215.3(f). Here, Respondent plainly conferred an economic benefit on Natale, the Bank's Chief Executive Officer and Chairman of the board of directors, when he caused the Bank to extend credit to or for the benefit of JDN FloPark, one of Natale's business interests.

a. Letters of Credit, Debit Authorizations, and Pledges of Securities to ACBB

In March 2008 and July 2008, ACBB issued letters of credit for the benefit of JDN FloPark and (nominally) [redacted] in the respective amounts of $250,000 and $500,000. In support of those letters, Respondent signed a letter agreement authorizing ACBB to debit the Bank's demand deposit account in the event of a draw on the letters of credit, and pledged $250,000 and $500,000 of the Bank's securities as collateral. Respondent also created a $250,000 line of credit at the Bank for JDN FloPark in March 2008, anticipating that ACBB, in the event of a draw on the letter of credit, would either debit the Bank's demand deposit account at ACBB or liquidate the Bank's securities, and the Bank would then debit JDN FloPark's line of credit, leaving JDN

FloPark (and not ACBB) responsible for repaying the Bank. (Tr. at 512-17.) (A $500,000 line of credit for [redacted] already existed when the $500,000 line of credit for JDN FloPark in July 2008, and the Bank did not replace that line of credit with a new line.) The securities were made available to ensure that ACBB would be repaid whether or not there were sufficient funds in the Bank's demand deposit account at ACBB. (Tr. at 282.)

The ALJ held that, because the letters of credit were not issued by the Bank itself and because the Bank pledged securities to ACBB, not to JDN FloPark, neither the letters nor the pledges constituted extensions of credit for purposes of Regulation O. (R.D. at 24-26.) Enforcement Counsel takes exception to this conclusion, and the Board agrees with Enforcement Counsel that the ALJ erred.[4]

Regulation O intentionally casts a wide net in defining an extension of credit; such an extension includes "[i]ssuance of a standby letter of credit (or other similar arrangement regardless of name or description)," various other loans and advances, and "[a]ny other similar transaction as a result of which a person becomes obligated to pay money (or its equivalent) to a bank, whether the obligation arises directly or indirectly." 12 C.F.R. § 215.3(a). Because, in each instance, the letter of credit, line of credit, debit authorization, and pledge of securities were inextricably linked—none of them would have occurred in isolation—they should be treated as a single transaction for these purposes, and the result of each transaction was unquestionably that JDN FloPark (acting through [redacted] as a nominee borrower in one instance) became obligated to pay the Bank (or would become obligated in specific circumstances outside of JDN FloPark's control or the Bank's control). (*See* Tr. at 52-53 (ACBB would not have issued letters of credit if

[4] The ALJ did not expressly address the authorization to debit the demand deposit account as an extension of credit under Regulation O, but the Notice of Charges addressed both the authorization and pledge (*see* Notice ¶¶ 22, 38), both were presented in the evidence and discussed at the hearing, and the Board finds that both were part of the extensions of credit for purposes of Regulation O.

the Bank had not pledged the securities to ACBB).) Therefore, the Board finds that the ALJ unnecessarily focused on whether a specific component of that transaction constituted an extension of credit. Furthermore, Regulation O specifically states that a letter of credit or a "similar arrangement" constitutes an extension of credit, and here the issuance of a letter of credit by ACBB on the Bank's behalf, with a mechanism in place (indeed, two alternative mechanisms) to transfer any indebtedness from ACBB to the Bank, appears to constitute a "similar arrangement" to a conventional single-institution letter of credit.

Past FDIC decisions have made it clear that Regulation O covers multi-component transactions and atypical extensions of credit. In *In the Matter of* ***, 1986 WL 379630 (FDIC Apr. 7, 1986), another bank extended credit to the respondent, and the bank where he worked purchased a participation in the loan without informing its board. The Board held that the purchase violated Regulation O, even though the initial extension of credit was made by a different institution—just as the letter of credit was nominally made by ACBB here. *Id.* at *6; *see also In the Matter of* ***, 1983 WL 207390, *7-8 (FDIC Dec. 5, 1983). In *In the Matter of* ***, 1986 WL 379633 (FDIC June 3, 1986), the respondent caused the bank to extend credit to his related interests and guaranteed the loan, both of which separately implicate Regulation O—but the FDIC Board treated the extension as a unitary transaction, just as the letter of credit, line of credit, debit authorization, and pledge of securities are properly viewed as a unitary transaction here. *Id.* at *2-3. And in *In the Matter of Ira Lee Brannan*, 1992 WL 812955 (FDIC April 14, 1992), the bank and its holding company, controlled by the respondent, filed consolidated tax returns, the bank paid the holding company for its estimated tax liability, and the payment proved to be in excess of the bank's actual tax liability. The bank never sought repayment (and the holding company funneled the overpayment to another of the respondent's

interests), and the Board found that "a de facto debtor-creditor relationship" between the bank and the holding company arose when the bank discovered the overpayment. *Id.* at *5. Here, there was a de facto debtor-creditor relationship between the Bank and JDN FloPark, acting in part through [redacted] that consisted of multiple documents and commitments, and it is proper to view those documents and commitments as a single transaction. *See also In the Matter of Ronald J. Grubb*, 1992 WL 813163, *17, *19 (FDIC Aug. 25, 1992) (letters of credit supported by the respondent's guarantee, and acceptance of deed in lieu of foreclosure to repay loans, constituted single transactions that violated Regulation O), *aff'd*, 34 F.3d 956 (10th Cir. 1994).

It is noteworthy as well that, under Regulation O, whenever the proceeds of a transaction are "used for the tangible economic benefit of the insider," that constitutes an extension of credit to the insider. 12 C.F.R. § 215.3(f)(1). Here, the proceeds of the letter agreement and the pledge of the Bank's securities—the Bank's funds and securities—were used to facilitate the creation of a letter of credit and fund the draw on the letter of credit, steps that unquestionably benefited Natale's interests. The issuance of the letter of credit allowed Natale to avoid immediate responsibility for funding the repairs required in the New Jersey litigation—the court accepted the letter of credit as proof that the plaintiff would receive the relief sought, or the equivalent in cash damages, and did not require Natale to pay the judgment up front. Thus, as long as they were "used for . . . [his] benefit," it is irrelevant whether the proceeds were transferred directly to Natale, and the commitment of the Bank's assets implicated Regulation O. *See Michael v. FDIC*, 687 F.3d 337, 354 (7th Cir. 2012) ("nominee loan to an insider" violated Regulation O regardless of the ostensible recipient of the proceeds); *Hutensky v. FDIC*, 82 F.3d 1234, 1240 (2d Cir. 1996) (loans to "nominal debtors" who transferred proceeds to insider interests violated Regulation O).

There is no question that the Bank's board of directors did not approve the letters of credit, debit authorization letter agreements, and the pledges of securities before the transactions were completed. Respondent does not contend otherwise.[5] Furthermore, there is no question that JDN FloPark was a related interest of Natale, or that the extension of $250,000 in credit to JDN FloPark in March 2008, and of $500,000 in credit (nominally to [redacted] in reality to JDN FloPark) in July 2008, exceeded the pertinent limitations on credit to insiders. Specifically, both of those transactions caused the Bank to exceed the $500,000 aggregated loan limit for insiders (meaning that full board approval of further credit was necessary), *see* 12 C.F.R. § 215.4(b)(2), and exceed the $100,000 aggregated loan limit for executive officers (whether or not the full board approved), *see* 12 C.F.R. § 215.5(c)(4). (*See also* Tr. at 74 (ACBB bank officer, testifying that ACBB's $500,000 letter of credit was for the benefit of JDN FloPark); Tr. at 321-23 (FDIC expert, testifying that extensions of credit benefited Natale).) Thus, the FDIC Board finds that those transactions violated Regulation O.[6]

b. $250,000 Line of Credit to JDN FloPark

To whatever extent the $250,000 line of credit to JDN FloPark is considered independently of the remainder of the $250,000 letter of credit transaction, the ALJ correctly found that the line of credit constituted a violation of Regulation O. (R.D. at 22-24.) The line of credit benefited Natale, and the Bank's board did not vote on or approve that extension of credit before it was extended.[7]

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[5] Respondent's disclosures to the Bank's Executive Loan Committee, and the Committee's approval of some aspects of the transactions, did not satisfy Regulation O, as the Committee did not have the power to act for the board. (Jt. Ex. 2 at 17, 47.)

[6] Furthermore, Natale's guarantee of the letter of credit constituted an extension of credit to him in violation of the aggregation limits. (FDIC Ex. 4; Tr. at 268-69.)

[7] The initial $500,000 line of credit ostensibly for the benefit of [redacted] was not included in the Notice of Charges as a violation of Regulation O, and the Board therefore does not consider whether it qualified

Respondent argues that, by including signature blocks for the board members in the Loan Approval Document (*see* Jt. Ex. 17 at 1), he showed his intent for the board to approve the extension of credit. (Respondent's Exceptions 18, 19.) That is irrelevant. Regulation O requires that, when credit is extended to a bank insider, a majority of the board must approve the extension "*in advance.*" 12 C.F.R. § 215.4(b)(1)(i) (emphasis added). Here, Respondent executed a note extending a line of credit to JDN FloPark on March 5, 2008—two days after he initially presented the request to the board—and no document in the record indicates that the board *ever* approved the request, let alone did so in that two-day window.[8] For similar reasons, Respondent's argument that the board "retroactively" approved the extension of credit (Respondent's Exceptions 18, 19), is both unsupported by the record—no document shows such a "retroactive" approval—and irrelevant. Regulation O requires approval in advance. Respondent's execution of the note without prior board approval violated Regulation O.

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independently as such a violation. The Board does address below whether the extension of that line of credit constituted an unsafe and unsound banking practice or a breach of fiduciary duty, however, as the Notice does allege that the Bank extended that credit without adequate assurance of repayment. (Notice ¶¶ 47-48.) The ALJ specifically held that the initial [redacted] line of credit was properly considered in this proceeding. Order on FDIC Motions in Limine at 3 (Aug. 11, 2014).

[8] Respondent also argues that a passing reference in another Bank document to this line of credit as "approved in March 2008" indicates approval of the line of credit at the appropriate time (Respondent's Exception 18; *see* Jt. Ex. 21 at 4), but the document did not say that the *board* approved it, and at any rate it did not state that the line was approved before March 5, as Regulation O requires.

Furthermore, the document in question asserts that the $250,000 line of credit "is a 100% participation with ACBB . . . and will only be used to provide funding for [a letter of credit] and as such, is not aggregated for Reg-O." (Jt. Ex. 21 at 4.) The mistaken views reflected in that document that Regulation O did not apply here because a line of credit intended to support a letter of credit is outside the purview of Regulation O, ACBB had purchased a true participation in the line of credit, or both, strongly suggest that the $250,000 line of credit was never submitted to the board at all. (*See also* Tr. at 297-98, 300 (Enforcement Counsel's expert, stating that Respondent's statement that Regulation O aggregation did not apply is incorrect).) Respondent later exacerbated the situation by recommending approval of additional extensions of credit to Natale and his related interests without citing the $250,000 and $500,000 letters of credit at all (Jt. Ex. 24; Tr. at 302-03), and failing to mention those letters when the Bank's counsel asked for a full accounting of extensions of credit to insiders. (Jt. Exs. 28, 29; Tr. at 303-06, 664.)

2. Unsafe and Unsound Practices

An unsafe and unsound banking practice is one that is "contrary to generally accepted standards of prudent operation" whose consequences are an "abnormal risk of loss or harm" to a bank. *Michael*, 687 F.3d at 352. An "imprudent act" posing an "abnormal risk of financial loss or damage to an institution, its shareholders, or the agencies administering the insurance funds" is an unsafe and unsound practice. *Seidman v. OTS*, 37 F.3d 911, 932 (3d Cir. 1994). Respondent's conduct met that standard.

a. Failure to Obtain and Maintain Adequate Assurances of Repayment

The ALJ found that Respondent, when he caused the Bank to pledge $250,000 in its Bank's securities to ACBB in March 2008 and $500,000 in the Bank's securities to ACBB in July 2008, acted imprudently and caused the Bank an abnormal risk of loss, because in neither event was the Bank adequately assured of repayment. (R.D. at 28-30.) The Board agrees, and further finds, consistent with the above, that the authorization to debit the Bank's demand deposit account posed the same risk. *See supra* n.4.

i. Failure to Ensure that the Bank Would Be Repaid if the Bank's Account Was Debited or the Securities Were Liquidated

Extending credit without ensuring that an adequate repayment agreement is in place constitutes an unsafe and unsound banking practice. *First State Bank of Wayne County v. FDIC*, 770 F.2d 81, 82 (6th Cir. 1985) ("extending credit that was not adequately secured" unsafe and unsound); *Gulf Fed. Sav. & Loan Ass'n v. FHLBB*, 651 F.2d 259, 264 (5th Cir. 1981) (legislative history of section 1818(e) indicates that "disregarding a borrower's ability to repay" is an unsafe and unsound practice); *In the Matter of the Stephens Security Bank*, 1991 WL 789326, *1 (FDIC Aug. 9, 1991) ("extending credit without adequate documentation . . . credit analysis . . . [or]

repayment agreements or failing to enforce repayment agreements" unsafe and unsound practice); *In the Matter of William Marvin Clark*, 1991 WL 757819, *4 (FDIC Jan. 29, 1991) (failure to "follow standard underwriting practices regarding the determination of a borrower's ability to pay based on current economic data" unsafe and unsound practice). When Respondent authorized ACBB to debit the Bank's deposit account at ACBB, and caused the Bank to pledge its securities to ACBB as collateral, he failed to take measures to ensure that the Bank would be repaid upon the debiting of the account or the liquidation of those securities, exposing the Bank to an abnormal risk of loss.

For both ACBB letters of credit, Respondent signed (a) a letter agreement authorizing ACBB to debit the Bank's demand deposit account, and (b) a security agreement pledging the Bank's securities to ACBB as collateral for the letters of credit. (Jt. Ex. 18 at 12, 18; Jt. Ex. 23 at 81, 84.) For both transactions, neither the letter agreement nor the pledge agreement was signed by the ostensible beneficiary of the letter of credit (JDN FloPark or [redacted] nor was there any separate commitment by the ostensible beneficiary to repay the Bank if ACBB debited the Bank's account or liquidated the Bank's securities. The promissory notes executed by those beneficiaries, creating lines of credit for them, did not link the lines of credit to the letter agreement or the security agreement at all, let alone expressly provide that the beneficiaries were required to repay the Bank upon the debiting of the demand deposit account or the liquidation of the securities. The pledge agreements are particularly notable in this respect because neither pledge agreement identifies *anything* that is secured by the pledges—the agreements contain two check-box alternatives identifying the obligation secured, but neither alternative was checked, and the agreements did not append any alternative option. (Jt. Ex. 18 at 12; Jt. Ex. 23 at 81.) Furthermore, the agreements gave ACBB broad authority to liquidate the securities whenever it

believed such liquidation was necessary to ensure repayment. (Jt. Ex. 18 at 13; Jt. Ex. 23 at 82 (liquidation permissible if ACBB "believe[s] that the prospect of due and punctual payment of any or all of the Obligations is impaired").) The Bank had no recourse against ACBB, JDN FloPark, [redacted] or anyone else in that event.

Respondent claims that the pledge of securities did not pose any risk to the Bank because he expected ACBB to debit the demand deposit account and return the securities, not liquidate them. (Respondent's Exceptions 20, 22.) The pledge agreements did not require ACBB to do so, however.[9] At any rate, it makes no difference for these purposes: the risk of nonrepayment arose equally from the letter agreement and the security agreement, as both agreements committed Bank assets to repay ACBB in the event the letters of credit were called, but failed to ensure that the ostensible borrowers would repay the Bank in turn. Hence, neither the $250,000 nor the $500,000 extension of credit was accompanied by an adequate assurance of repayment.[10]

ii. Use of a Nominee Borrower

The Bank's extensions of credit in connection with the $500,000 ACBB letter of credit were particularly problematic because [redacted] not JDN FloPark, was identified as the debtor on the line of credit, even though JDN FloPark was the true beneficiary. Even if the Bank did debit [redacted] line of credit in the event of a draw on the letter of credit, JDN FloPark had no obligation to repay the Bank in that event. Indeed, when that very thing happened, JDN FloPark did not repay the Bank. (Nor did [redacted] The ALJ correctly concluded that the use of [redacted] as a nominee borrower was an unsafe and unsound practice. (R.D. at 26-27.)

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[9] Indeed, ACBB ultimately liquidated the securities pledged in support of the $500,000 letter of credit, converted them to a certificate of deposit, and cashed the certificate of deposit when the letter was called, rather than debiting the demand deposit account. (Jt. Exs. 33, 36.)

[10] The ALJ concluded, and the Board agrees, that Respondent's conduct did not pose an abnormal risk of loss to ACBB. (R.D. at 28.) It did pose an abnormal risk of loss to the Bank, however.

The record shows that [redacted] obtained the line of credit from the Bank in September 2007 as a nominee or straw borrower for JDN FloPark. In particular, the Loan Approval Document that Respondent presented to the board described the line of credit as benefiting [redacted] father rather than [redacted] herself, and the letter of credit that the Bank initially issued did not even mention [redacted] (Jt. Ex. 10 at 2; Jt. Ex. 13.) Notably, the loan was initially requested by other parties—including Natale—while [redacted] was out of the country (Jt. Exs. 5, 6), and [redacted] mother stated that "Joe's office is preparing the letter of explanation and Joe's lawyer . . . is preparing the" letter of credit. (Jt. Ex. 8.) The Bank's origination fees were paid from a JDN FloPark address. (Jt. Ex. 12 at 2.) And when Respondent later requested approval for a line of credit to support the $250,000 ACBB letter of credit for JDN FloPark, he described the request as an increase on the earlier $500,000 letter—i.e., the letter that was nominally for [redacted] as if JDN FloPark had been the intended beneficiary all along:

> In 2007, the Bank approved a similar facility to [redacted] ($500,000), daughter of [redacted] who was engaged to construct the properties in the JDN development. . . . Subsequently, the amount requested has been increased to $750,000, resulting in our seeking approval for the $250,000 balance.

(Jt. Ex. 17 at 2.) Respondent acknowledged that this language reflected his awareness, as of March 3, 2008, that the [redacted] and JDN FloPark letters of credit were inextricably linked. (Tr. at 649-52.) ACBB's internal memorandum regarding the $500,000 letter of credit it issued likewise strongly suggests that the true beneficiary was JDN FloPark, not [redacted] as the memorandum describes the letter as arising from a court's order that "JDN Properties at Florham Park, LLC needed to complete repairs" on the plaintiff's property, and simply notes that [redacted] father, had agreed to carry out the repairs. And an ACBB officer confirmed at the hearing that the $500,000 letter of credit ACBB issued was for the benefit of JDN FloPark. (Tr.

at 29, 74.)[11]

Later documents confirm that Natale was the true beneficiary of the extension of credit to [redacted] and that Respondent was aware of that fact. In June 2008, for instance, Respondent replied to the proposed replacement of the Bank's letter of credit for [redacted] with an ACBB letter of credit, also nominally for [redacted] and the e-mail's subject line read "JDN Properties at Florham Park, LLC." (Jt. Ex. 22.) Respondent certainly knew at that point that JDN FloPark had an interest in the [redacted] letter of credit. Similarly, in October 2008, Respondent confirmed in an internal e-mail that the $250,000 and $500,000 letters of credit should be viewed as a unitary transaction. (Jt. Ex. 26.) Again, nothing in the record indicates that Respondent learned of [redacted] nominee status only after the fact, or notified the board that he had been misled.

Nominee loans are considered inherently unsafe and unsound practices, as they mislead the lender about the true identity of the borrower and thus the risk incurred in extending credit. *See, e.g., In the Matter of Tonya D. Williams*, 2015 WL 3644010, *7 (FDIC Apr. 21, 2015); *In the Matter of Donald E. Hedrick*, 1996 WL 772762, *7 (OCC 1996); *In the Matter of John K. Snyder*, 1996 WL 33414773 (OCC 1996). This case offers a particularly striking example of the dangers of nominee loans, as [redacted] did not repay the loan when the letter of credit was called and ultimately sued ACBB, contending that the letter of credit was issued without her consent. (Jt. Ex. 23 at 2; Jt. Ex. 36; Tr. at 93.)

iii. Failure to Link Promissory Notes to ACBB's Letters of Credit

Furthermore, even assuming that [redacted] was a real and not simply a nominal party to the

[11] Respondent contends that ACBB's internal memorandum does not reflect any conversations with him (Respondent's Exception 12), but does not explain where ACBB would have obtained its information about the transaction other than from Respondent. At any rate, the internal memorandum suggests that the true beneficiary of the letter of credit was JDN FloPark, and Respondent's extensive familiarity with the transaction makes it unlikely that he was unaware of those facts.

$500,000 letter and line of credit, Respondent did not take the requisite steps to ensure that she would repay the Bank under those instruments. The promissory note creating a line of credit that [redacted] executed on September 25, 2007 was tied (albeit loosely) to the *Bank's* letter of credit issued that same date, and was never updated to link to *ACBB's* letter of credit issued nearly a year later. That note stated:

> Line of Credit is being given to facilitate issuance of a Letter of Credit by Borrower to Mark L. Breitman, [unreadable] beneficiary, 260 Route 34, Matawan, NJ 07747.

(Jt. Ex. 23 at 65.) Enforcing this ambiguous language would have been problematic even for the original letter of credit issued by the Bank, as the ALJ noted. (R.D. at 28-29.) [redacted] was identified as the "Borrower," but there was no Letter of Credit "by" Borrower, and identifying Breitman—the attorney for JDN FloPark—as the "beneficiary" confused the matter even more. And simply stating, as the note did, that the line of credit "facilitate[d] issuance of a Letter of Credit" did not in itself obligate [redacted] to make repayments in the event of a draw on the letter of credit.[12] Even assuming that this language gave rise to an obligation by [redacted] regarding the *Bank's* September 25, 2007 letter of credit, however, the language could not reasonably have been read to create the same obligation with regard to *ACBB's* July 15, 2008 letter of credit. [redacted] could properly have objected that she was not required to repay draws on a letter of credit that did not even exist when she signed the note. The ALJ found (R.D. at 29), and the Board agrees, that Respondent did not obtain a meaningful assurance of repayment when he authorized ACBB to debit the Bank's demand deposit account, and caused the Bank to pledge $500,000 in securities to ACBB, to support ACBB's letter of credit for [redacted]

The same is true of the $250,000 Bank line of credit for JDN FloPark: the note

[12] The note's references to a "Loan Agreement" and to "Loan Documents" that apparently never existed confused matters even further, as the ALJ noted. (R.D. at 29 n.32.)

establishing the line of credit did not meaningfully assure repayment for the Bank because it was not clearly linked to ACBB's letter of credit, as the ALJ noted. (R.D. at 28.) The only reference to the letter of credit in the note was this: "PURPOSE: the purpose of this loan is LOC TO SUPPORT LETTER OF CREDIT." (Jt. Ex. 18 at 9.) No specific letter of credit was mentioned, and the note does not provide that JDN FloPark was required to repay the Bank if ACBB liquidated the Bank's securities or debited the Bank's demand deposit account. It does not address what events will be deemed to constitute a draw on JDN FloPark's line of credit. Therefore, Respondent's contention (Respondent's Exception 10) that the ALJ erred in finding "no evidence of an agreement between the Bank and JDN FloPark to pay $250,000 to the Bank if the [letter of credit] was called and the marketable securities pledged were liquidated" (R.D. at 11 n.16) has no merit: the note does not constitute such an agreement. The ALJ correctly concluded that the sloppy paperwork Respondent executed was an unsafe and unsound practice.[13]

iv. Failure to Renew the [redacted] Promissory Note and Line of Credit

As to the ACBB $500,000 letter of credit, Respondent exacerbated the Bank's exposure and engaged in unsafe and unsound practices by allowing the [redacted] note and line of credit to lapse, as the ALJ concluded. (R.D. at 30-31.) That note and line expired on September 25, 2008 (Jt. Ex. 23 at 65), and Respondent failed to arrange for their renewal, despite ACBB's repeated warnings that it needed to obtain updated financial information for [redacted] including a

[13] Respondent's expert, Cheryl Richards, claimed that the lines of credit could have been drawn down if the letters of credit were called, and thus that the Bank had an assurance of repayment, but Ms. Richards did not look at the specific language of either of the notes. (Tr. at 514-15, 535-36.) Testimony in the abstract about what could have happened does not address whether the paperwork created in these specific transactions was adequate to assure repayment for the Bank, as the ALJ noted. (R.D. at 36.) The loss sustained by the Bank here strongly indicates that it was not.

modification of the promissory note to extend through July 15, 2009, and despite the Bank's internal reminder system. (Tr. at 615-16; R.D. at 16; Jt. Ex. 32.) Following the expiration of the promissory note and line of credit, neither [redacted] nor anyone else had any obligation to repay the Bank in the event of a draw on the $500,000 ACBB letter of credit (which remained in force, and was automatically renewed each year long after the note and line expired, *see* Jt. Ex. 23 at 87), and in the event of ACBB's liquidation of the pledged Bank securities or debiting of the Bank's demand deposit account at ACBB. It could hardly be clearer that Respondent's failure to obtain a new promissory note left the Bank without adequate assurances of repayment.[14]

Respondent argues that the [redacted] promissory note did not, in fact, expire because it included the words "on demand," Respondent's Exception 1, but misreads the note. It stated that it matured "ON DEMAND as provided in Note, or no later than September 24, 2008." (Jt. Ex. 23 at 65.) The note provided elsewhere that [redacted] could be required to repay any draws "ON DEMAND." The plain meaning of the note is that the Bank could require repayment of any draws "on demand" rather than waiting until September 24, 2008, and Respondent's argument that the "on demand" language meant that the note had no termination date at all—i.e., that the September 24, 2008 maturity date was meaningless—is not persuasive. The witness that offered this interpretation was Respondent's expert, Cheryl Richards, and she had no personal knowledge of the intent of the parties to the note. (Tr. at 518.)[15]

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[14] Respondent also permitted the $250,000 JDN FloPark line of credit to lapse, though the likelihood of harm to the Bank from that failure was somewhat lower because, unlike the $500,000 [redacted] letter of credit, the $250,000 JDN FloPark letter of credit also expired and was not renewed. (Jt. Ex. 18 at 15; Jt. Exs. 30, 31.) While the Bank's debit authorization letter agreement and pledge of securities did not expire, and the terms of the pledge agreement were sufficiently ambiguous that ACBB could conceivably have liquidated those securities for unrelated purposes, the Board does not find that allowing the $250,000 line of credit to lapse posed an abnormal risk of loss to the Bank.

[15] Respondent also claims that he did not draft or review the [redacted] promissory note, Respondent's Exception 13, but as he presented to the Committee a Loan Approval Document referencing the line of

For the same reason, Respondent's argument that the pledging of securities did not pose a risk of loss to the Bank (Respondent's Exception 22) is flatly contradicted by the facts of this case. Respondent cites testimony from Ms. Richards that the securities could have been returned to the Bank if ACBB had debited the Bank's demand deposit account, and the Bank had then debited the borrower's line of credit in a corresponding amount, and pursued the borrower for repayment under the promissory note, minimizing the risk of loss to the Bank. (Tr. at 514-18.) But that was only possible if the note still existed and was enforceable against the borrower, and because [redacted] was a nominee borrower and the note had expired, that option was not available when the $500,000 ACBB letter of credit was in fact called. As noted above, it made little difference what repayment avenue ACBB chose (debiting the Bank's demand deposit account, or liquidating the Bank's securities), as the Bank did not have a meaningful assurance of repayment by [redacted] (or JDN FloPark) in either event.

Respondent also argues that the existence of a second mortgage on [redacted] vacation home constituted an assurance of repayment. (Brief in Support of Respondent's Exceptions at 13.) But that mortgage secured [redacted] obligations under the promissory note, obligations whose enforceability was, to say the least, problematic even before the note expired—and once the note expired on September 25, 2008, the mortgage was irrelevant:

[T]he mortgage is merely security for the debt and without a subsisting debt or

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credit created in that promissory note (Jt. Ex. 10 at 1), it would have been extremely reckless for him to seek the Committee's approval of a document he never read. At any rate, Respondent's duties included the supervision of lending officers, and failure to supervise subordinates may constitute an unsafe and unsound banking practice and a breach of fiduciary duty. *See, e.g., In the Matter of Larry B. Faigin*, 2015 WL 9855325, *82 (FDIC Dec. 15, 2015); *Leuthe*, 1998 WL 438323, *13; *In the Matter of James G. Welk*, 1992 WL 813217, *9 (FDIC June 5, 1992) (Recommended Decision); *In the Matter of* ***, 1988 WL 583064, *9 (FDIC Mar. 1, 1988). Respondent's contention that he was not responsible for ensuring the renewal of the promissory note (Respondent's Exception 13) fails for the same reason, as does his more general argument that he was not responsible for any of the flaws in the pertinent transactional documents because he may not have seen them. (Respondent's Exception 22.)

> obligation, the mortgage has no efficacy. Thus, when the underlying obligation fails, the mortgage becomes a nullity.

Great Falls Bank v. Pardo, 622 A.2d 1353, 1357 (N.J. Ch. Div. 1993), *aff'd*, 273 N.J. Super. 542, 642 A.2d 1037 (N.J. App. Div. 1994). The mortgage itself simply states that it secures the line of credit:

> This Second Mortgage is granted to secure the following: [T]he performance and observance by [redacted] (the "Borrower"), of Borrower's obligations to the Mortgagee under the following instruments All line of credit agreements. . . . or other similar agreements or arrangements related to the foregoing by and between the Borrower and the Mortgagee, of even date w1th this Mortgage, in the aggregate maximum principal sum of $500,000.00 (the "Loan") including without limitation all obligations from time to time of the Borrower to the Mortgagor on account of (i) letters of credit issued *by the Mortgagee* for the account of the Borrower . . . .

(Jt Ex. 23 at 74 (emphasis added.) The Bank could not legitimately foreclose on collateral when the previously secured obligation (the promissory note) no longer existed, and the reference to a letter of credit issued "by the Mortgagee" was obviously not sufficient to obligate [redacted] when a letter of credit was issued by *another* institution—i.e., ACBB. The ALJ concluded, and the Board agrees, that the lapse of the note made the mortgage irrelevant. (R.D. at 31.)

Respondent cites Ms. Richards's testimony that the mortgage secured all of [redacted] debts, not merely the promissory note (*see* Respondent's Exception 13), but the mortgage did not so provide. Ms. Richards stated:

> I believe the bank was protected. It had a lien on the mortgage. It still had its lien. It still had its lien position even if the note hadn't expired in one of the paragraphs in the mortgage and still got right of offset with your borrower's debt and expenses.

(Tr. at 518.) Ms. Richards was apparently relying on this language:

> [The Mortgage secures] the payment, performance and observance by Mortgagor of each and every covenant, condition and obligation contained in this Mortgage or referred to herein, or incurred in connection herewith; and the payment of all other indebtedness now or hereafter owing by Borrower to Mortgagee . . . evidenced by a promissory note or other similar agreements or arrangements

related to the foregoing or agreement signed by Borrower, whether or not otherwise secured.

(Jt. Ex. 23 at 74.) This piece of confusing testimony about an even more confusing provision is scant evidence that the Bank had a meaningful assurance of repayment, and at any rate the specific language does not support Ms. Richards's assertion.

- The mortgage secured "each and every covenant, condition and obligation contained in this Mortgage or referred to herein." The mortgage did not, of course, "refer to" the later-executed ACBB letter of credit or the Bank's pledge of securities.
- The mortgage secured obligations "incurred in connection herewith." It is questionable, at best, whether the Bank would have been able to enforce the mortgage against [redacted] on the theory that the later-executed letter of credit and pledge—about which [redacted] contended she was not consulted; no record evidence indicates that she was—constituted an "obligation . . . incurred in connection" with the mortgage.
- The mortgage secured "all other indebtedness now or hereafter owing by Borrower to Mortgagee evidenced by a promissory note or other similar agreements or arrangements related to the foregoing or agreement signed by Borrower." Once the promissory note expired, it is likewise uncertain, to say the least, whether ACBB's letter of credit and the Bank's pledge gave rise to a "similar agreement[] or arrangement[] related to" any existing agreements signed by [redacted] Again, [redacted] did not sign, or even acknowledge, the creation of any of those documents, and nothing in the record suggests that she was consulted about them.

The ambiguous language cited by Ms. Richards did not, on its face, make the mortgage of [redacted] property an adequate assurance of repayment.[16]

v. Inadequate Underwriting

Aside from the concerns about whether anyone was *legally obligated* to repay the loans, Respondent's conduct constituted an unsafe and unsound banking practice because he caused the Bank to extend credit without adequately evaluating the borrowers' *ability* to repay the loans. Specifically, Respondent represented to the Committee that [redacted] debt-to-income ratio was approximately 25 percent, which complied with the 40 percent cap imposed by Bank policy—but that computation improperly combined [redacted] income with her husband's income, even though [redacted] was the sole signatory on the promissory note. (Jt. Ex. 10 at 1; Jt. Ex. 11; Jt. Ex. 23 at 8-12; Tr. at 223-25, 229-31.) [redacted] income, by itself, was not enough to repay a draw on the line of credit. (Tr. at 230-31, 236-37.) Had only [redacted] income been considered, the debt-to-income ratio would have been more than 60 percent before the $500,000 extension of credit, and more than 80 percent afterwards, raising significant concerns about the prospect of repayment. (Tr. at 233-37.) Failure to properly underwrite a loan by accurately evaluating the borrower's ability to repay constitutes an unsafe and unsound practice. *Clark*, 1991 WL 757819, *10.

Nor did the second-lien mortgage on [redacted] vacation property remedy the concerns about the prospects of repayment. Collecting on such a lien would have been a difficult and lengthy undertaking, and would have required the Bank to buy out the first lien—a significant

[16] Respondent's speculation that a subordinate employee failed to put the [redacted] promissory note into the Bank's "tickler" system, and therefore Respondent did not receive notice of the expiration (*see* Respondent's Exception 23), is not supported by any evidence—the record does not show whether there was a "tickler" entry for the note—and is unpersuasive in any event. As noted above, failure to supervise subordinates is an unsafe and unsound practice.

up-front expense—in order to foreclose on the second. (Tr. at 77-78, 586-87.) The uncertain prospects of any such foreclosure made reliance on the mortgage alone as a source of repayment, in these circumstances, an unsafe and unsound practice.[17]

As for the $250,000 line of credit to JDN FloPark, the ALJ correctly concluded that Respondent did not obtain adequate assurances of repayment because the line was unsecured. (R.D. at 31.) Natale did give a personal guarantee indicating that he had net worth in excess of $40 million and $173,000 in excess annual cash flow, but the underlying information dated from 2006 and 2007, and Respondent apparently did not seek updated information. (R.D. at 31; Jt. Ex. 19 at 6.) Thus, Respondent failed to obtain adequate assurances of repayment for that line.[18]

Finally, Respondent argues that the FDIC did not adequately notify him in the proceedings below that it viewed the failure to obtain adequate assurances of repayment as misconduct justifying a prohibition under 12 U.S.C. § 1818(e). (Brief in Support of Respondent's Exceptions at 9; *see also* Respondent's Exception 20.) The Board disagrees. The Notice of Charges stated that the $500,000 extension of credit "posed more than the normal risk that it would not be repaid," and further noted that that the $250,000 line of credit was unsecured. (Notice ¶¶ 31, 48.) The FDIC's Prehearing Statement contended that Respondent's steps to ensure repayment of the $250,000 were inadequate:

> a) ACBB, as the participant, never advanced any money to the Bank, as the lender;

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[17] The ALJ also cited an ongoing decline in the real estate market at the time of these events as further evidence that Respondent's reliance on a second-lien mortgage on [redacted] property was unsafe and unsound. (R.D. at 30 n.33, 31.) No evidence was presented on that decline as it affected real estate in New Jersey, however, and thus the Board does not rely on it.

[18] Respondent argues that ACBB also deemed Natale's assets and cash flow sufficient (Respondent's Exception 24), but ACBB's concurrence does not make Respondent's conduct proper, particularly when, in light of Respondent's commitment of Bank assets, ACBB had no true exposure and no incentive to do a thorough underwriting job.

b) ACBB's right to repayment upon the draw of the LoC was immediate and unrelated to whether the Bank was repaid first;

c) The Bank had no recourse against Natale/JDN LLC to obtain repayment upon a potential draw of the ACBB $250,000 LoC; and

d) Conover caused the Bank to retain all the risk of an unsecured line of credit that was only guaranteed by Natale.

(FDIC Prehearing Statement at 10.) The Prehearing Statement was also explicit that Respondent caused the Bank to extend the $500,000 credit without adequate assurances of repayment:

(a) ACBB, as the participant, never advanced any money to the Bank, as the lender;

b) Because Conover had posted Bank assets as collateral, ACBB's right to repayment upon the draw of the LoC was immediate and unrelated to whether the Bank was repaid first (despite the fact that the collateral for the $500,000 [redacted] line of credit was [redacted] shore house);

c) Bank had no recourse against [redacted] to obtain repayment upon the draw of the ACBB $500,000 LoC because there was no draw on the Bank's issuance of the [redacted] line of credit; and

d) Conover caused the Bank to retain all the risk of the line of credit to [redacted] while securing ACBB's interests by posting Bank assets as collateral.

(FDIC Prehearing Statement at 11.) Enforcement Counsel was required to put Respondent on notice of the facts alleged to constitute unsafe and unsound practices, and it did so here.[19] Thus, Respondent was on notice that Enforcement Counsel viewed this behavior as misconduct warranting prohibition.[20]

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[19] To be sure, the Notice was not as explicit as it could have been in identifying the specific aspects of these transactions that gave rise to inadequate assurances of repayment, but Enforcement Counsel was required only to put Respondent "on notice of the facts alleged to constitute an unsafe or unsound practice," *Seidman*, 37 F.3d at 939 n.40, and Enforcement Counsel did so here: it identified Respondent's conduct in causing the Bank to extend credit as an unsafe and unsound practice. It was not required to explain all the reasons why that conduct was unsafe and unsound.

[20] Respondent also argues that Enforcement Counsel took the position that underwriting violations were not part of this case (Respondent's Exception 20), but that argument was rejected by the ALJ. Specifically, Enforcement Counsel sought, in a motion *in limine*, to bar Respondent's attempts to bolster

b. Misleading Statements about ACBB's Participation

Enforcement Counsel argued in its post-hearing brief that Respondent engaged in unsafe and unsound practices when he made misleading statements to the Bank's Executive Loan Committee about ACBB's role in the transactions. Specifically, Respondent submitted documents to the Committee characterizing the $250,000 ACBB letter of credit transaction as a 100 percent participation by ACBB, even though ACBB did not purchase an interest in the loan and bore none of the ultimate risk. (Jt. Ex. 17 at 1; Jt. Ex. 18 at 2.)[21] The ALJ found that these misrepresentations were contrary to prudent banking practices, but also found that they did not cause an abnormal risk of loss to the Bank or add to the already-existing abnormal risk of loss. (R.D. at 32.) We agree.

A loan participation is a "contractual arrangement between a lender and a third party, whereby the third party, labeled a participant, provides funds to the lender," and the lender then provides funds to the borrower. *Natwest USA Credit Corp. v. Alco Std. Corp.*, 858 F. Supp. 401, 407-08 (S.D.N.Y. 1994). A true participation agreement arises when, *inter alia*, "(1) money is advanced by a participant to a lead lender; (2) the participant's right to repayment only arises when the lead lender is paid;" and "(3) only the lead lender can seek legal recourse against the borrower." *In re AutoStyle Plastics, Inc.*, 269 F.3d 726, 737 (6th Cir. 2001). A loan participation "'allows a lending institution to share the *lending risk*.'" *Id.* at 736 (emphasis

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his case by putting on evidence of his underwriting process. The ALJ denied Enforcement Counsel's motion *in limine* in pertinent part, stating that "the underwriting of the lines of credit, which were a potential source of repayment, is relevant." (Order on FDIC Motions in Limine at 3 (Aug. 11, 2014).) Given that holding, nothing barred Enforcement Counsel from countering Respondent's argument by offering evidence that Respondent's underwriting was inadequate. Respondent therefore had ample notice that underwriting was part of this case; indeed, Respondent argued as much, and Respondent's expert, Ms. Richards, testified about the adequacy of Respondent's underwriting. (Tr. at 514-24.)

[21] Respondent also signed a document describing the $500,000 ACBB letter of credit transaction as a 100 percent loan participation agreement, but nothing in the record indicates that that document was given to the Committee. (Jt. Ex. 23 at 57.)

added) (quoting W.H. Knight, Jr., *Loan Participation Agreements: Catching Up With Contract Law*, 1987 Colum. Bus. L. Rev. 587, 589 (1987)). Courts have viewed a sharing of lending risk as the *sine qua non* of loan participation agreements. *In re Woodson Co.*, 813 F.2d 266, 271 (9th Cir. 1987) (where lender "relieved the permanent investors of all risk of loss," there was no participation agreement between the lender and investors); *In re Sackman Mortgage Corp.*, 158 B.R. 926, 933 (Bankr. S.D.N.Y. 1993) ("In determining whether a transaction is a loan or a participation agreement, courts have generally viewed the risk allocation as the most significant factor, finding that agreements whereby the 'participant' bears no risk of loss constitute debtor-creditor relationships in the form of loans rather than true participation agreements."). The transactions here did not fit that description, as ACBB advanced no funds to purchase a participation and retained none of the risk that loans would not be repaid. *See also* Tr. at 37-38 (ACBB officer, testifying that "[i]n most scenarios where we buy an interest in a loan, we would wire or put money in a bank's –lead bank's account . . . . This was unique in that we were issuing a letter of credit, so we didn't buy a participation per se.").

This is not a mere semantic quibble. On their face, Respondent's representations that ACBB had a 100 percent participation in the loans presented a picture diametrically opposite from reality. Respondent was claiming, in effect, that ACBB bore *all* of the risk, when ACBB in fact bore *none* of it. (*See* Tr. at 280-83, 575-76.) The misrepresentation was significant, and Respondent has offered nothing to justify it.[22]

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[22] Respondent contends that there was no misrepresentation because the Loan Approval Document disclosed a $250,000 increase in "Total Exposure" to Natale. (Respondent's Exception 26.) At best, however, that statement, alongside the repeated assertion that ACBB would have a 100 percent participation interest, confused the situation; combined, those two statements appeared to suggest that the Bank had a nominal additional exposure of $250,000 but a true exposure of $0. Respondent offered no evidence that the board understood that the Bank was assuming all of the loan risk. Respondent also disputes the ALJ's conclusion that the "participation agreements" were contrary to generally accepted

Nevertheless, nothing in the record indicates that these misrepresentations were material to the Committee's approval of these transactions. Misrepresentations must be material to constitute unsafe and unsound banking practices. *See, e.g., In the Matter of Constance C. Cirino*, 2000 WL 1131919, *45 (FDIC May 10, 2000); *In the Matter of John R. DiBella*, 1995 WL 399085, *3 (FDIC May 3, 1995). The materiality showing was not made: there was no testimony at the hearing suggesting that, had Respondent represented ACBB's "participation" more accurately, the Committee would have viewed the loans differently. Given the confusing and self-contradictory nature of the statements at issue, *see supra* n.22, the absence of such testimony makes it difficult to determine whether the statements were material. Furthermore, the record shows that the abnormal risk of loss arose from the failure to assure repayment, and does not indicate that Respondent's statements to the Committee enhanced that risk. Thus, in these circumstances, Respondent's misrepresentations did not, in themselves, constitute an unsafe and unsound banking practice.

3. Breaches of Fiduciary Duties

The foregoing misconduct constituting regulatory violations and unsafe and unsound practices also constituted breaches of Respondent's fiduciary duties to the Bank. Directors and officers of banks have fiduciary duties to act in the best interests of the institution. *See FDIC v. Appling*, 992 F.2d 1109, 1113 (10th Cir. 1993). Fiduciary duty refers to the level of care that "ordinary prudent and diligent men would exercise under similar circumstances." *In the Matter of Larry B. Faigin*, 2015 WL 9855325, *82 (FDIC Dec. 15, 2015) (citations omitted).

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standards of prudent bank operation (R.D. at 32), but that conclusion was supported by testimony from an ACBB officer, who stated that the terms of the "participation" in this case did not fit with his experience (Tr. at 37-39, 131-32), and from Enforcement Counsel's expert, who testified that the "100% participation" representation was not consistent with the Bank's retention of the risk of loss. (Tr. at 279-83, 289-90, 297-300.)

Obligations encompassed within fiduciary duty for a bank officer include "safeguarding the bank's property, complying with state and federal banking laws and regulations, and ensuring that the bank is operated properly," and requires, *inter alia*, "proper supervision of subordinates" and "a knowledge of state and federal banking laws," along with "constant concern for the safety and soundness of the bank." *In the Matter of* ***, 1988 WL 583064, *9 (FDIC 1988). Furthermore, failures to disclose material information, "even if not asked," may constitute a breach of fiduciary duty. *De La Fuente v. FDIC*, 332 F.3d 1208, 1222 (9th Cir. 2003) ("De La Fuente had a fiduciary duty to disclose everything he knew relating to the transaction."). The ALJ found, and the Board agrees, that Respondent's conduct did not meet these standards. (R.D. at 32-35.)

As described above, Respondent presented loans for approval without taking meaningful steps to ensure repayment and caused the Bank to violate Regulation O by extending credit to an insider and his related interests. Notably, Respondent approved lines of credit to [redacted] and JDN FloPark with little if any assurance that money drawn on the lines would be repaid, and exacerbated the [redacted] credit situation by allowing the line to lapse. Extending credit without adequate assurances of repayment constitutes a breach of fiduciary duty. *Leuthe*, 1998 WL 438323, *12; *In re Matter of* ***, 1988 WL 583065, *8 (FDIC Apr. 25, 1988).

Respondent also made misrepresentations to the Bank's Executive Loan Committee. As noted above, he made misleading statements about ACBB's "participation" interest in the loans. In addition, Respondent did not disclose to the Committee that the initial $500,000 Bank line of credit, ostensibly for [redacted] was in fact for Natale's benefit; rather, he claimed that it was for the benefit of [redacted] father, without mentioning Natale's role in the New Jersey litigation. (Jt. Ex. 10 at 2.) Respondent claims that he was not aware of the benefit to Natale at

that time, Brief in Support of Respondent's Exceptions at 6-7, but that is not credible given his subsequent description (in March 2008) of the $250,000 letter of credit for JDN FloPark (after the court increased the required amount to $750,000) as an "increase" over the earlier letter, "resulting in our seeking approval for the $250,000 balance." (Jt. Ex. 17 at 2.) Respondent appears to have viewed the $500,000 letter of credit for [redacted] and the $250,000 letter of credit for JDN FloPark as an integrated whole. Nothing in the record indicates that Respondent informed the board or the Committee that he had only recently learned about the true beneficiary of the initial '[redacted] letter of credit and line of credit, or that he acknowledged that the letter and line had been obtained without full board approval, in violation of Regulation O. Furthermore, the ALJ heard testimony from Respondent on this point (Tr. at 612), and found his assertions not credible. (R.D. at 19.) The ALJ has "broad discretion" in making credibility judgments, *see, e.g.*, *Williams*, 2015 WL 3644010, *11; *In the Matter of Steven D. Haynes*, 2014 WL 4640797, *13 (FDIC July 15, 2014), *aff'd*, --- F. App'x ---, 2016 WL 6247134 (9th Cir. Oct. 26, 2016), and nothing on the face of the record indicates that the ALJ abused that discretion here.[23]

Respondent also failed to disclose to the Committee that he was pledging the Bank's securities to ACBB. In support of ACBB's $250,000 letter of credit to JDN FloPark and

[23] Respondent's assertion that he was not even aware that Natale benefited from the transactions by March 2009, *see* Respondent's Exception 29, is even less credible. Notably, an e-mail to Respondent in June 2008 addressed the replacement of the Bank's $500,000 letter of credit for [redacted] with an ACBB letter of credit, and the e-mail's subject line read "JDN Properties at Florham Park, LLC," belying Respondent's assertions that he did not know of Natale's interest in the letter. (Jt. Ex. 22.) In October 2008, in response to an internal e-mail requesting details about "that letter of credit which ACBB provided and we . . . secured," Respondent responded: "$500M for the [redacted] LOC and $250M for Joe's mortgage company." (Jt. Ex. 26.) Respondent conspicuously did *not* say that the two letters of credit were separate extension of credit to different persons or entities; rather, he confirmed that, properly understood, they were a single extension of credit artificially divided between [redacted] and Natale's company.

$500,000 letter of credit to [redacted] Respondent signed documents pledging $250,000 and $500,000 in the Bank's marketable securities. (Jt. Ex. 18 at 12; Jt. Ex. 23 at 81.) The Loan Approval Document submitted in support of the $250,000 letter of credit does not mention that pledge (Jt. Ex. 17 at 2), and there is no record of *any* disclosure to the Committee or the board regarding the July 2008 $500,000 letter of credit and the accompanying pledge of the Bank's securities. Respondent's failure to candidly disclose the nature of the Bank's extensions of credit breached his duty of care. *See Haynes*, 2014 WL 4640797, *12 ("lack of candor" with loan committee breached duty of care); *In the Matter of Chad W. Friese*, 2012 WL 7186316, *1 (FDIC July 20, 2012) (concealment of conduct from bank board breached fiduciary duty); *In the Matter of Henry P. Massey*, 1993 WL 853757, *5 (FDIC Oct. 5, 1993) (concealment of information from bank's loan committee constituted breach of fiduciary duty); *In the Matter of Michael D. Landry*, 1999 WL 440608, *12 (FDIC May 25, 1999), *aff'd*, 204 F.3d 1125 (D.C. Cir. 2000) (officers' failure to disclose personal interests in transactions breached fiduciary duties);. Nor did Respondent inform the Bank that he was authorizing ACBB to debit the Bank's demand deposit account. (Jt. Ex. 18 at 18; Jt. Ex. 23 at 84.)[24] The record therefore reflects numerous examples of Respondent's breaches of his fiduciary duty to the Bank.[25]

4. Statute of Limitations

Respondent argues that any misconduct relating to the $250,000 Bank line of credit and

[24] Respondent claims that he was not required to inform the Committee of the pledge because he had the power to pledge the Bank's securities as collateral. (Respondent's Exception 7.) The cited document does not appear to support that assertion—it gives Respondent powers with regard to the Bank's checking account and does not mention the Bank's securities (Jt. Ex. 27 at 6)—and at any rate the document certainly does not prove that Respondent had the power to pledge the Bank's securities *without informing the Bank*, as appears to have occurred here.

[25] Respondent also claims that the board could have learned of the pledging through securities reports, Respondent's Exception 7, but the witness that testified to that effect was an expert who had no personal knowledge of the Bank's practices and made assumptions based on other banks' practices (Tr. at 577-79), and Respondent did not offer any evidence of such reports.

ACBB letter of credit for JDN FloPark, both issued in March 2008, fell outside the five-year statute of limitations set forth in 28 U.S.C. § 2462, as the FDIC did not file its Notice of Charges against Respondent until July 12, 2013. (Brief in Support of Respondent's Exceptions at 4-8.)[26] The ALJ rejected this argument, finding that Respondent's misconduct with regard to this line of credit and letter of credit constituted a continuing violation. (Order Denying Respondent's Motions in Limine (Aug. 11, 2014) at 2.)

The ALJ's holding was correct. A continuing violation occurs when a defendant creates a situation from which new claims continue to arise, notwithstanding that some of the defendants' specific acts fell outside the limitations period. *See, e.g., Leuthe*, 1998 WL 438323, *5; *see also Courtney v. La Salle Univ.*, 124 F.3d 499, 505 (3d Cir. 1997) ("[I]n the case of a continuing unlawful practice, every day that the practice continues is a fresh wrong for purposes of the statute of limitations.") (citations omitted). Courts have held that, where a violation gives rise to new statutory penalties each day it persists, a new claim accrues on each of those days for purposes of the continuing violation doctrine. *See, e.g., United States v. Edelkind*, 525 F.3d 388, 396 (5th Cir. 2008); *National Parks Conservation Ass'n v. TVA*, 480 F.3d 410, 419 (6th Cir. 2007); *InterAmericas Investments, Ltd. v. Board of Governors*, 111 F.3d 376, 382 (5th Cir. 1997); *Wyatt v. FAA*, 28 F.3d 111, 1994 WL 273999, *1 (9th Cir. June 20, 1994). Violations of Regulation O, unsafe and unsound banking practices, and breaches of fiduciary duty give rise to civil penalties "for each day during which such violation, practice, or breach continues." 12 U.S.C. § 1818(i)(2)(A), (B). Furthermore, the statutes of limitation governing FDIC

[26] Because, as set forth below, the Notice of Charges was timely as to the JDN FloPark transaction under the five-year limitations period set forth in § 2462, the Board does not consider whether that provision does in fact govern here. *See In the Matter of Billy Proffitt*, 1998 WL 850087 (FDIC Oct. 6, 1998), *7-9 (six-year limitations period set forth in 12 U.S.C. § 1818(i)(3) governs removal and prohibition proceedings), *rev'd*, 200 F.3d 855 (D.C. Cir. 2000); *In the Matter of James L. Leuthe*, 1998 WL 438324, *3-4 (FDIC Feb. 13, 1998) (same), *aff'd*, 1999 WL 334497 (D.C. Cir. 1999).

enforcement actions are strictly construed in favor of the FDIC. *In the Matter of James L. Leuthe*, 1998 WL 438324, *6 (FDIC Feb. 13, 1998) (Recommended Decision), *aff'd*, 1999 WL 334497 (D.C. Cir.1999); *see also In the Matter of Interamericas Investments Ltd.*, 1996 WL 193671 (FRB Apr. 9, 1996), *aff'd*, 111 F.3d 376 (5th Cir. 1997) (same).[27]

In this case, Respondent's conduct was not undone or corrected before the five-year limitations period began. The $250,000 line of credit for the benefit of Natale remained open past July 12, 2008, and Respondent never sought approval from the full board for that line of credit. Nor did Respondent remedy the features of that line of credit that made it an unsafe and unsound practice and a breach of fiduciary duty, notably the lack of security and the failure to candidly disclose the pertinent details to the board. Thus, Respondent's misconduct with respect to the $250,000 ACBB line of credit persisted through, and past, July 12, 2008, and the Notice of Charges as to that transaction was timely.

Effects

The record supports the ALJ's conclusion that the Bank suffered both an enhanced risk of loss and an actual loss as a result of Respondent's acts. (R.D. at 38-40.) A "reasonably foreseeable" loss, or increased risk of loss, satisfies the "effects" requirement. *Kaplan v. OTS*, 104 F.3d 417, 421 (D.C. Cir. 1997); *FDIC v. Bierman*, 2 F.3d 1424, 1434 (7th Cir. 1993). That a

[27] Respondent cites *De La Fuente* for the proposition that Regulation O violations are not "continuing." (Brief in Support of Respondent's Exceptions at 6.) But it does not appear that the significance of daily penalties was raised in *De La Fuente*, and at any rate that decision did not address whether unsafe and unsound practices and breaches of fiduciary duty can be continuing violations. *See also Leuthe*, 1998 WL 438324, *5-6 (applying continuing violation theory in removal proceeding based in part on Regulation O violations, unsafe and unsound practices, and breaches of fiduciary duty).

Respondent also argues that the penalty provisions are significant only as to the civil money penalty claim (Brief in Support of Respondent's Exceptions at 8), but the court in *Interamericas* considered a similar provision in finding a continuing violation for purposes of both a civil money penalty and a cease and desist order. 111 F.3d at 381. Furthermore, it would be anomalous to view the same conduct as a continuing violation for purposes of one remedy but not for another. *See Leuthe*, 1998 WL 438323, *5 (applying continuing violation approach to both prohibition and civil money penalty actions).

loss was caused in part by other circumstances does not preclude a finding of causation; the conduct at issue need not be the proximate cause of the loss. *Landry v. FDIC*, 204 F.3d 1125, 1139 (D.C. Cir. 2000); *In the Matter of Jeffrey Adams*, 1997 WL 805273, *5 (FDIC Nov. 12, 1997) ("That others might have contributed to the Bank's loss does not absolve Weitz of liability in a case brought pursuant to section 8(e) of the FDI Act.")

The "effects" requirement is easily satisfied here because the Bank did suffer a loss in the amount of $587,263. The $500,000 ACBB letter of credit for the benefit of [redacted] was called on February 25, 2011, and ACBB made a full payment and liquidated the Bank's securities to reimburse itself. (Jt. Exs. 34-36.)[28] ACBB also debited $87,263 from the Bank's demand deposit account to reimburse itself for expenses incurred in defending a suit by [redacted] contesting the validity of the letter of credit. (Jt. Ex. 36.)[29] At that point, of course, the Bank had no recourse against [redacted] as the line of credit and promissory note had expired, and an attempt to foreclose on [redacted] vacation property was dismissed because the property was already subject to forfeiture. (Resp. Exs. 4, 5.) Respondent argues that his conduct did not cause the Bank's losses because the FDIC could have pursued remedies in the forfeiture proceeding (Respondent's Exception 23), but the record does not show that any relief was available in that proceeding,[30] and at any rate Respondent's conduct was plainly a contributing cause in the loss. *Adams*, 1997

[28] For reasons that are not explained in the record, ACBB had already liquidated the securities and was holding the proceeds as a certificate of deposit. (Jt. Ex. 33.) It cashed the certificate of deposit when the letter of credit was called. (Jt. Ex. 36.)

[29] Respondent also claims, citing Ms. Richards's testimony, that a fee-shifting provision in the promissory note required [redacted] to pay the Bank's fees and costs incurred in connection with the Bank's enforcement of obligations under the note. (Respondent's Exception 30; Tr. at 546-47, 552-55.) But that provision expired with the rest of the note, and at any rate ACBB's fees and costs were incurred in connection with [redacted] suit against ACBB, not the Bank's enforcement of the note (or the mortgage). Nothing in the note, or anywhere else, required [redacted] to pay *ACBB's* fees and costs.

[30] The cited document refers to proceedings in a civil forfeiture case after the mortgaged property was seized by the United States , and does not show that any relief was in fact available, or has in fact been obtained, by any party in the civil forfeiture proceeding. (Resp. Ex. 6 at 11-18.)

WL 805273, *5 (respondent's conduct need not be the sole or proximate cause of losses; loss causation can be shown even if "multiple factors, and individuals, may contribute to a bank's losses"); *see also Faigin*, 2015 WL 9855325, *83 ("It has long been clear that there may be more than one cause of harm to a bank, and that an individual need not be the proximate cause of the harm in order to be held liable under Section 8(e)."); *In the Matter of* * * *, 1985 WL 303871, *114 (FDIC Aug. 19, 1985) (Enforcement Counsel need only show a "nexus," not "proximate cause"). Specifically, Respondent, by arranging for the $500,000 ACBB renewable letter of credit and failing to arrange for a renewed line of credit to support the letter, caused the Bank to pay $500,000 to ACBB when the letter was called, and the circumstances that prevented the Bank from recouping that loss by foreclosing on the collateral do not make Respondent's role irrelevant. Respondent also argues that he could not have foreseen the dismissal of the foreclosure action and the failure to recover in the forfeiture action (Brief in Support of Respondent's Exceptions at 13-14), but the Bank's inability to enforce its lien was foreseeable as soon as the promissory note expired, if not before then.

Respondent also claims that he could not have foreseen the payment of attorney's fees to ACBB (Brief in Support of Respondent's Exceptions at 18), but the Loan Participation Agreement required the Bank to indemnify ACBB for losses suffered as a result of the Bank's breaches of the Agreement, and [redacted] suit appears to have arisen, in part, from Respondent's mismanagement of the [redacted] line of credit. (Jt. Ex. 23 at 59; Jt. Ex. 36; Tr. at 93.) Respondent could easily have foreseen that failing to obtain [redacted] consent to the new letter of credit, and allowing [redacted] promissory note to expire, would interfere with the administration of that loan and impede any attempt to enforce [redacted] purported obligations.

Furthermore, even assuming that the actual loss incurred was not attributable to

Respondent's conduct, the Board discussed above the many features of these transactions that diminished the prospects of repayment and thus elevated the foreseeable risk of loss. In particular, Respondent executed documents authorizing the Bank to debit the Bank's demand deposit account and pledging the Bank's securities to ACBB as collateral, but the governing documents did not require JDN FloPark or [redacted] to repay the Bank if the letters were called and ACBB debited the Bank's account or liquidated those securities. Respondent's failure to provide enforceable mechanisms through which the Bank could seek repayment created a risk of loss that Respondent could, and should, have foreseen.[31]

Culpability

Culpability, for purposes of section 1818(e), can be shown by "personal dishonesty" or a "willful or continuing disregard for the safety and soundness of the financial institution." 12 U.S.C. § 1818(e)(1). Both of those standards are satisfied here.

1. Personal Dishonesty

The ALJ concluded, and the Board agrees, that Respondent displayed "personal dishonesty" in the transactions discussed above. (R.D. at 41.) Personal dishonesty is shown by "a disposition to lie, cheat or defraud; untrustworthiness; lack of integrity; misrepresentation of facts and deliberate deception by pretense and stealth; or want of fairness and

[31] The ALJ also found that Respondent subjected the Bank to an elevated risk of loss by allowing the $250,000 ACBB letter of credit for JDN FloPark and the associated line of credit to expire on March 5, 2009 (R.D. at 40), but the Board agrees with Respondent that such an expiration, by itself, did not expose the Bank to risk. (Respondent's Exception 27.) Because *both* the letter of credit and line of credit expired, ACBB was not required to honor the letter of credit if it were called after March 5, 2009, and accordingly ACBB was not likely to liquidate the Bank's securities—even if the poor drafting of the pledge agreement made that possible—or debit the Bank's demand deposit account in that event. *See supra* n.14. Falling out of compliance with a court order to obtain $750,000 in letter of credit may have been an unwise move for JDN FloPark, but that did not make it unduly risky for the Bank. Likewise, failing to include a renewal clause in the letter of credit in the first place may have been imprudent for JDN FloPark, but it did not bear on Respondent's fiduciary duty to the Bank.

straightforwardness." *Van Dyke v. Board of Governors*, 876 F.2d 1377, 1379 (8th Cir. 1989). Misleading statements to, or withholding of material information from, bank directors constitutes personal dishonesty. *De La Fuente*, 332 F.3d at 1224 (concealment of information from board); *Greenberg v. Board of Governors*, 968 F.2d 164, 171 (2d Cir. 1992) (failure to disclose insider transactions to board). Respondent's conduct fits the description of personal dishonesty.

Respondent failed to disclose to the board that the [redacted] letters and line of credit would benefit Natale, and did not alert the board even when, he admitted, he "started to believe" in March 2008 that the [redacted] letter and line of credit, approved several months before, were related to the JDN FloPark letter and line. (Tr. at 651.) The evasive wording of the Bank's letter of credit for [redacted] (which never mentions her at all, *see* Jt. Ex. 13)—and the circumstances of the request (Natale requested the letter from Respondent at a time when [redacted] was not even in the country, *see* Jt. Exs. 5, 6, and Natale's office prepared the documents, *see* Jt. Ex. 8)—suggest that Respondent knew full well at the time that [redacted] was not the true beneficiary of that letter, (Jt. Ex. 13), but Respondent did not candidly disclose that fact to the board or the Committee. Respondent then exacerbated the situation by authorizing ACBB to debit the Bank's demand deposit account and pledging the Bank's securities in support of the ACBB $500,000 letter of credit, again ostensibly for [redacted] benefit, without informing the board or the Committee of the connection to Natale. Respondent had multiple opportunities to inform the board and the Committee of the insider transactions, and passed on each opportunity:

1. In September 2007, Respondent presented the Bank's $500,000 letter of credit and line of credit for [redacted] to the Committee.
2. In January 2008, Respondent presented a $250,000 increase in the $500,000 letter of credit for [redacted] to the Committee.

3. In March 2008, Respondent presented the $250,000 ACBB letter of credit and line of credit to the board.

4. In June 2008, ACBB approached Respondent about replacing the $500,000 Bank letter of credit for [redacted] with an ACBB letter of credit, and Respondent signed a loan participation agreement, authorized the debiting of the Bank's demand deposit account, and pledged the Bank's securities, but Respondent did not discuss that matter with the board or Committee at all.

Respondent's lack of candor with the board and Committee on Natale's connection to these transactions reflected personal dishonesty.

Respondent also failed to disclose, or misrepresented, other aspects of these transactions. Respondent represented that ACBB would have a "100%" participation interest in the loans. (*See, e.g.*, Jt. Ex. 17 at 1.) That was not accurate: in view of Respondent's letter agreement authorizing debit of the Bank's demand deposit account, and Respondent's pledge of the Bank's securities, ACBB did not retain any risk of nonrepayment, which is not consistent with a participation agreement. A more accurate description would have been that ACBB nominally issued the letters of credit but the Bank retained all of the pertinent risk, but Respondent did not state as much to the board or the Committee. Those misrepresentations likewise reflected personal dishonesty.

2. Willful or Continuing Disregard

"Willful or continuing disregard" requires a showing of Respondent's scienter as to the harm to the Bank resulting from his actions. *See, e.g.*, *De La Fuente II*, 332 F.3d at 1223 ("willful disregard" refers to "deliberate conduct which exposed the bank to abnormal risk of loss or harm contrary to prudent banking practices"); *Cavallari v. OCC*, 57 F.3d 137, 145 (2d

Cir. 1995) (a "willingness to turn a blind eye to [the bank's] interest in the face of known risk" constitutes willful disregard); *Grubb v. FDIC*, 34 F.3d 956, 962 (10th Cir. 1994) ("continuing conduct" is "that conduct which is voluntarily engaged in over a period of time with heedless indifference to the consequences"); *Williams*, 2015 WL 3644010, *10 (same). An officer acts "willfully" when he is aware of his conduct; "willfulness" does not require a showing that Respondent was aware of the law. *In the Matter of Michael D. Landry*, 1998 WL 34083421 (FDIC Aug. 14, 1998), *aff'd*, 204 F.3d 1125 (D.C. Cir. 2000).[32]

"Continuing disregard" refers to "'a mental state akin to recklessness.'" *Kim v. OTS*, 40 F.3d 1050, 1054 (9th Cir. 1994) (quoting *Brickner v. FDIC*, 747 F.2d 1198, 1203 & n.6 (8th Cir. 1984)). Respondent's conduct was both "continuing" and reckless, as the ALJ found. (R.D. at 42-43.) He caused the Bank to issue the $500,000 line of credit for [redacted] in September 2007, caused the Bank to issue the $250,000 JDN FloPark line of credit and commit Bank assets in support of the $250,000 ACBB line of credit for JDN FloPark in March 2008, and caused the Bank to commit Bank assets in support of the $500,000 ACBB line of credit for [redacted] in July 2008. Furthermore, he allowed the [redacted] line of credit to lapse while the $500,000 ACBB letter of credit remained in place from September 2008 through September 2009, when he left the Bank. Respondent's conduct was therefore "continuing," and as discussed above, Respondent knew or should have known that his conduct exposed the Bank to an abnormal risk

[32] For this reason, Respondent's argument that there was no evidence that he knowingly caused the Bank to violate the law (Respondent's Exception 21) is irrelevant; the ALJ did not so find, and did not need to. Rather, the ALJ found that Respondent "knowingly and intentionally caused the Bank to issue" a $250,000 extension of credit to JDN FloPark" (R.D. at 23), which the record supports and Respondent does not dispute. Furthermore, the Board has rejected "lack of knowledge" defenses to Regulation O violations, holding that bank fiduciaries who have a duty to ascertain the salient facts about a transaction cannot claim lack of knowledge as an excuse. *In the Matter of* ***, 1983 WL 207390, *6 (FDIC Dec. 5, 1983) ("Respondents argue their lack of knowledge as to the true facts on July 16, 1981, as a defense. Ignorance under such circumstances is not a valid defense. It was their duty to know the facts.").

of loss, and proceeded anyway. *See In the Matter of Ramon M. Candelaria*, 1997 WL 211341, *6 (FDIC Mar. 11, 1997) ("continuing disregard" shown by two nominee loans over a period of six months), *aff'd*, 1998 WL 43167 (10th Cir. Feb. 3, 1998); *In the Matter of Frank E. Jameson*, 1990 WL 711218, *8 (FDIC June 12, 1990) (two incidents of falsifying loan records within three months constituted "continuing disregard"), *aff'd*, 931 F.2d 290 (5th Cir. 1991).

The ALJ also concluded, and the Board agrees, that Respondent's conduct was "willful," as the acts in question were undertaken deliberately and were committed even though Respondent knew or should have known that they posed an abnormal risk of loss to the Bank. (R.D. at 41-42.) *See, e.g.*, *Cavallari*, 57 F.3d at 145 ("deliberately and consciously tak[ing] part in an action that evidences utter lack of attention to an institution's safety and soundness" constitutes willful disregard); *In the Matter of Charles F. Watts*, 2002 WL 31259465, *8 (FDIC Aug. 6, 2002) (conduct is willful if it is "practiced deliberately with full knowledge of the facts and risks"); *In the Matter of Lawrence A. Swanson*, 1995 WL 329616, *5 (OTS Apr. 4, 1995) (willful disregard shown by "demonstrated awareness or prior warnings that the conduct at issue was unsafe or unsound"). Examples include falsifying business records, *see, e.g.*, *Hendrickson v. FDIC*, 113 F.3d 98, 103 (7th Cir. 1997), check-kiting schemes, *see, e.g.*, *Van Dyke v. Board of Governors*, 876 F.2d 1377, 1380 (8th Cir. 1989), and extending credit to insolvent companies. *In the Matter of* ***, 1988 WL 583065, *9 ("Respondent * * * approved the overdrafts knowing that the funds would be used as working capital for * * *, a company he knew or should have known to be insolvent or in danger of insolvency.").

Respondent's failure to obtain the renewal of [redacted] promissory note is particularly notable in this regard, as ACBB specifically requested that Respondent obtain a renewed

promissory note, and Respondent never did so. (Jt. Ex. 19 at 12-14.)[33] ACBB also asked Respondent for updated financial information on [redacted] on multiple occasions, and Respondent did not provide that either. (Jt. Ex. 19 at 12-14; Jt. Ex. 22.) The result, of course, was an actual loss when the $500,000 ACBB letter of credit for [redacted] was called, ACBB liquidated the Bank's securities, and the Bank could not obtain repayment from [redacted] and Respondent's conduct greatly enhanced the risk of that loss—and Respondent's inaction in the face of such an obvious risk suggests a "willingness to turn a blind eye to [the Bank's] interest." *Cavallari*, 57 F.3d at 145. Respondent's other failures to obtain an adequate assurance of repayment, as detailed above, likewise indicate deliberate conduct, and Respondent knew, or should have known, that that conduct exposed the Bank to an abnormal risk of loss. *See De La Fuente*, 332 F.3d at 1223-24 ("placing the bank's assets in danger" by relying on "inferior collateral" constituted willful disregard).

Respondent's failure to obtain board approval for the letters of credit also indicates willfulness, as Respondent knew or should have known that the board must approve in advance extensions of credit exceeding an aggregate of $500,000 to bank insiders (a threshold that Natale had already passed), *see* 12 C.F.R. § 215.4(b)(2), and Respondent executed documents extending the Bank's credit without waiting for such board approval. (Jt. Ex. 18 at 2, 9, 12; Jt. Ex. 23 at 60, 81.) Respondent also knew or should have known that the Bank could not, in any circumstances, approve an extension of credit to an executive officer exceeding $100,000 for purposes other than housing or education, and yet Respondent caused the Bank to extend credit exceeding that threshold expressly for the benefit of Natale's business interests (the $250,000

[33] Respondent claims that he did not open ACBB's reminder e-mail (Respondent's Exception 15), but does not explain why he did not do so. Failing to open an e-mail from a business partner does little to negate the charge that Respondent participated in unsafe and unsound banking practices and breached his fiduciary duty to the Bank.

line of credit and commitment of Bank assets), and through a nominee borrower, [redacted] (the $500,000 line of credit and commitment of Bank assets). *See Hedrick*, 1996 WL 772762, *7 (obtaining a nominee loan without a candid disclosure to the board, and "continued failure to disclose the nature of the arrangement at the time of the further extensions of credit," indicated willful and continuing disregard).

Respondent's lack of candor with the Bank, as discussed above in connection with the "personal dishonesty" factor, likewise reflects willful or continuing disregard. In *In the Matter of Hal J. Shaffer*, 2009 WL 1677055 (FDIC Apr. 23, 2009), for example, the Board held that "misrepresenting or failing to disclose facts to the Bank to conceal" Regulation O violations constitutes willful and continuing disregard. *Id.* at *6; *see also In the Matter of Robert Michael*, 2010 WL 3849537, *10 (FDIC Aug. 10, 2010) ("arranging and facilitating . . . nominee loans while misrepresenting or failing to disclose facts to the Bank to conceal their related interests" constitute willful and continuing disregard"), *aff'd*, 687 F.3d 337 (7th Cir. 2012); *In the Matter of Roque de la Fuente*, 2004 WL 614659, *5 (FDIC Feb. 27, 2004) (deliberate violations of Regulation O, and "deliberate steps - including knowingly misrepresenting facts to the Bank's board and to FDIC examiners - to conceal . . . related interests," indicated willful and continuing disregard), *aff'd*, 156 F. App'x 44 (9th Cir. 2005).

Respondent argues that the record did not reflect that he "deliberately exposed the bank to abnormal risk of loss or harm" (Brief in Support of Respondent's Exceptions at 3), but that is not the standard. The conduct itself must be deliberate (rather than "technical or inadvertent," *see Oberstar v. FDIC*, 987 F.2d 494, 503 (8th Cir. 1993)), but Enforcement Counsel is not required to show that Respondent intended to harm the Bank. *See, e.g., Brickner*, 747 F.2d at 1202 (FDIC need not "establish that petitioners intentionally did something to endanger the

safety of their bank"). Respondent's conduct was plainly deliberate, nor accidental, and Respondent knew or should have known at the time that his conduct posed an elevated risk of loss to the Bank. That is sufficient to satisfy the "willful or continuing disregard" requirement. For the same reason, Respondent's argument that the culpability analysis is not a "strict liability standard" (Respondent's Exception 39, Brief in Support of Respondent's Exceptions at 16) attacks a straw man: the ALJ did not so hold, and there was ample evidence that Respondent's conduct met the scienter standard required for the culpability analysis.

The Board therefore adopts the ALJ's recommendation that an Order of Removal and Prohibition be entered against Respondent.

B. The CMP Assessment is Appropriate.

Civil money penalties (CMPs) are imposed to "serve as deterrents to violations of laws, rules, regulations and orders of the agencies." *Long v. Board of Governors*, 117 F.3d 1145, 1154 (10th Cir. 1997); *In the Matter of Richard D. Donohoo*, 1995 WL 618673, *27 (FDIC July 5, 1995) (CMPs authorized to "deprive the violators of any financial benefit derived as a result of the violations, provide a sufficient degree of punishment, and [establish] an adequate deterrent to the respondents and others from future violations of banking laws and regulations"), *aff'd in pertinent part sub nom. Lindquist & Vennum v. FDIC*, 103 F.3d 1409 (8th Cir. 1997). The ALJ recommended a second-tier CMP of $25,000, and the evidence in the record supports that penalty.

A second-tier CMP is appropriate where there has been (1) misconduct in the form of, *inter alia*, reckless engagement in an unsafe or unsound practice in conducting a financial institution's affairs, or a breach of a fiduciary duty, and (2) effects which include either a pattern of misconduct, or conduct which caused or was likely to cause more than minimal loss to the

institution, or which resulted in a gain or benefit to the respondent. 12 U.S.C. § 1818(i)(2(B); *see, e.g., Leuthe,* 1998 WL 438323, *16-17. A second-tier CMP carries a penalty of up to $37,500 for each day the violation continues. 12 U.S.C. § 1818(i)(2)(B); 12 C.F.R. § 509.103.

The Board has already discussed Respondent's unsafe and unsound banking practices and breaches of fiduciary duty and the effects of those acts and need not repeat that discussion here. Section 8(i) requires, however, that any unsafe and unsound banking practice be conducted "reckless[ly]" for a second-tier CMP to be imposed. The Board finds that standard is met here. Recklessness is established by acts committed "in disregard of, and evidencing conscious indifference to a known or obvious risk of a substantial harm." *Cavallari*, 57 F.3d at 142; *see also Simpson v. OTS*, 29 F.3d 1418, 1425 (9th Cir. 1994) (similar definition of "recklessness").

Respondent approved letter of credit transactions that violated Regulation O without obtaining adequate assurances that the Bank would be repaid if the letters were called, both because the repayment obligations were not properly articulated in the governing documents and because the underwriting of the loans was deficient. The risk of substantial harm to the Bank from default on those loans was "known or obvious," and Respondent's repeated approvals of the letter of credit transactions indicated, at the very least, "conscious indifference" to that risk. Certainly, Respondent had more than enough information to raise concerns about the potential risk arising from the loans as approved—and, as an experienced loan officer, Respondent had more than enough knowledge to understand the importance of ensuring a reliable source of repayment. Respondent just did not act on that information. Respondent's failure to take elementary steps to ensure that there would be a borrower with repayment obligations, and that the borrower in question had the capacity to repay, was reckless conduct that caused, and posed a risk of, substantial loss to the Bank.

As for the amount of the CMP, Respondent is responsible for up to $37,500 for each day his violations persisted uncorrected. *United States v. Marine Shale Processors*, 81 F.3d 1329, 1357 (5th Cir. 1996). As Respondent's misconduct began in September 2007 and continued until September 2009, a CMP could potentially greatly exceed the $25,000 penalty recommended by the ALJ. Other relevant considerations in setting the amount of a CMP include Respondent's financial resources and good faith, the gravity of the violation, and Respondent's history of previous violations. The ALJ concluded that Respondent's financial resources and the harm to the Bank (nearly $600,000 in losses) support a significant CMP, and he found that Respondent did not act in good faith given his failure to apprise the Committee of the nature of the state-income construction loans. The ALJ also found no history of prior violations, and cited certain factors set forth in interagency guidance as relevant. (R.D. at 46-48; *see* Interagency Policy Regarding the Assessment of Civil Money Penalties by the Federal Financial Institutions Regulatory Agencies, 63 Fed. Reg. 30226-02.) Specifically, the ALJ cited the following factors identified in the interagency guidance as supporting augmentation of the CMP:

> (1) Evidence that the violation or practice or breach of fiduciary duty was intentional or was committed with a disregard of the law or with a disregard of the consequences to the institution;
> (2) The duration and frequency of the violations, practices, or breaches of fiduciary duty;
> . . .
> (6) Any threat of loss, actual loss, or other harm to the institution, including harm to the public confidence in the institution, and the degree of such harm;
> (8) Any restitution paid by the respondent for the losses; [and]
> (12) Tendency to engage in violations of law, unsafe or unsound banking practices, or breaches of fiduciary duty.

(R.D. at 68.) The above discussion of Respondent's misconduct fully supports the ALJ's conclusion regarding the applicability of these factors. The ALJ also cited the following factors as mitigating the CMP:

(9) Any history of previous misconduct, particularly where similar to the actions under consideration; and
(10) Previous criticism of the institution or individual for similar actions;

(*Id.*) Likewise, the ALJ properly identified these as mitigating factors, given that nothing in the record reflects any similar previous misconduct by Respondent, nor had the Bank been criticized for similar actions in the past. The Board adopts the ALJ's recommendation of a $25,000 CMP.

C. Respondent's Exceptions

Respondent filed 51 exceptions to the Recommended Decision challenging numerous aspects of the ALJ's findings of fact and legal conclusions. Those exceptions do not raise any factual or legal errors or point to any discrepancies in the record establishing that either the prohibition order or the CMP assessment is not warranted. To the extent that they are pertinent to matters already addressed, the Board has in the context of the discussion above disposed of certain exceptions. Respondent's remaining exceptions are addressed following.

Some of Respondent's exceptions challenge the ALJ's credibility judgments. *See* Exceptions 4, 16. As discussed above, however, the ALJ is empowered to assess the credibility of witnesses appearing before him, and the Board will reverse those judgments only if the ALJ abused his discretion. Nothing in the record indicates that he did so. In Exception 4, for instance, Respondent contends that the ALJ should have credited Respondent's testimony about a conversation Respondent purportedly had with his subordinate, [redacted] in which [redacted] stated that neither he nor Respondent was aware of Natale's connection to these transactions. Other documents in the record support the ALJ's conclusion that this testimony is not credible—for instance, Respondent's acknowledgment just a few months later that the $250,000 JDN FloPark letter of credit was an increase on the $500,000 '[redacted] letter of credit—and the Board does not believe that the ALJ abused his discretion in declining to credit

Respondent's claims. For the same reason, the Board finds unpersuasive Respondent's argument in Exception 16 that the ALJ erred in refusing to credit Respondent's testimony that he was unaware of the connections between Natale and the [redacted] transaction.

Exceptions 2, 3, 4, 5, 6, 9, 11, 16, and 35 challenge various minor factual findings or omissions in the ALJ's Recommended Decision, or cite what Respondent believes to be additional material facts. None of these disputes materially affect the ALJ's ultimate factual conclusions regarding the nature of Respondent's conduct, and they do not affect the Board's decision to adopt the ALJ's Recommended Decision. *See Landry*, 1999 WL 440608, *30.

Exceptions 8, 14, and 20 question certain factual findings made by the ALJ. The Board, however, has reviewed the cited evidence and finds sufficient evidence in the record to support each of the contested findings.

Exception 25 argues that the ALJ erred in finding that the increase in the letters of credit from $500,000 to $750,000 increased the risk to the Bank, but the ALJ did not so hold. Rather, the ALJ held that the court-ordered increase in the amount of the letter of credit should have put Respondent on notice that the construction defects at issue in the litigation were serious, and that there was a nontrivial possibility that the letters of credit would be called. (R.D. at 31.) Respondent does not dispute that point.

Exceptions 17, 27-34, 36-38, and 40-51 largely recapitulate other exceptions and need not be addressed separately.

D. Enforcement Counsel's Exceptions

Enforcement Counsel submits two exceptions to the ALJ's Recommended Decision, contending that the ALJ erred in concluding that the pledging of securities does not constitute an extension of credit, and further erred in holding that the letters of credit issued by ACBB do not

constitute an extension of credit by the Bank. As set forth above, the Board agrees. Because Regulation O defines an extension of credit broadly, it is proper to view the $250,000 and $500,000 transactions as an integrated whole, and Respondent was required to obtain board approval before proceeding with those transactions. He did not.

V. CONCLUSION

After a thorough review of the record in this proceeding, and for the reasons set forth previously, the Board finds that an Order of Prohibition and Assessment of a CMP is warranted against Respondent. In this case, the record plainly shows that Respondent, over a period of approximately two years, put the Bank at risk by approving letters of credit to a nominee borrower, by extending credit to an insider in violation of Regulation O, and by putting Bank funds at risk with little assurance of repayment. In view of this conduct, the Board is persuaded that Respondent should be permanently barred from the banking industry. Finally, in light of the entire record, the Board finds that the CMP imposed is appropriate and consistent with the statute's intended effects.

Based on the foregoing, the Board affirms the Recommended Decision of the ALJ and adopts in full the conclusions of law and findings of fact therein, to the extent they are consistent with this Decision, and issues the following Orders implementing its Decision.

ORDER TO PROHIBIT

The Board of Directors of the FDIC, having considered the entire record of this proceeding and finding that Respondent Douglas V. Conover, formerly the senior vice president and business banking manager of First State Bank, Cranford, New Jersey, engaged in unsafe or unsound banking practices and breaches of his fiduciary duties resulting in loss to the Bank and a personal benefit to him, and that his actions involved willful and continuing disregard for the safety and soundness of the Bank, hereby ORDERS and DECREES that:

1. Douglas V. Conover shall not participate in any manner in any conduct of the affairs of any insured depository institution, agency or organization enumerated in section 8(e)(7)(A) of the FDI Act, 12 U.S.C. § 1818(e)(7)(A), without the prior written consent of the FDIC and the appropriate federal financial institutions regulatory agency as that term is defined in section 8(e)(7)(D) of the FDI Act, 12 U.S.C. § 1818(e)(7)(D).
2. Douglas V. Conover shall not solicit, procure, transfer, attempt to transfer, vote, or attempt to vote any proxy, consent or authorization with respect to any voting rights in any financial institution, agency, or organization enumerated in section 8(e)(7)(A) of the FDI Act, 12 U.S.C. § 1818(e)(7)(A), without the prior written consent of the FDIC and the appropriate federal financial institutions regulatory agency, as that term is defined in section 8(e)(7)(D) of the FDI Act, 12 U.S.C. § 1818(e)(7)(D).
3. Douglas V. Conover shall adhere to all voting agreements with respect to any insured depository institution, agency, or organization enumerated in section 8(e)(7)(A) of the FDI Act, 12 U.S.C. § 1818(e)(7)(A), except as otherwise permitted, in writing, by the FDIC and the appropriate federal financial institutions regulatory agency, as that term

is defined in section 8(e)(7)(D) of the FDI Act, 12 U.S.C. § 1818(e)(7)(D).

4. Douglas V. Conover shall not vote for a director, or serve or act as an institution-affiliated party, as that term is defined in section 3(u) of the FDI Act, 12 U.S.C. § 1813(u), of any insured depository institution, agency, or organization enumerated in section 8(e)(7)(A) of the FDI Act, 12 U.S.C. § 1818(e)(7)(A), without the prior written consent of the FDIC and the appropriate federal financial institutions regulatory agency, as that term is defined in section 8(e)(7)(D) of the FDI Act, 12 U.S.C. § 1818(e)(7)(D).
5. This ORDER shall be effective thirty (30) days from the date of its issuance.

ORDER TO PAY CIVIL MONEY PENALTY

The Board, having considered the entire record in this proceeding, and taking into account the appropriateness of the penalty with respect to the size of the financial resources and good faith of Respondent, the gravity of the violations and such other matters as justice may require, hereby ORDERS and DECREES that:

1. A civil money penalty is assessed against Douglas V. Conover in the amount of $25,000 pursuant to 12 U.S.C. § 1818(i).
2. This ORDER shall be effective and the penalties shall be final and payable thirty (30) days from the date of its issuance.

The provisions of these ORDERS will remain effective and in force except to the extent that, and until such time as, any provision of these ORDERS shall have been modified, terminated, suspended, or set aside by the FDIC.

IT IS FURTHER ORDERED that copies of this Decision and Orders shall be served on Counsel for Respondent Douglas V. Conover, Enforcement Counsel, the ALJ, and the

Commissioner of the New Jersey Department of Banking and Insurance.

By direction of the Board of Directors.

Dated at Washington, D.C. this 13th day of December, 2016.

/s/
Robert E. Feldman
Executive Secretary

(SEAL)

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