



**Comptroller of the Currency
Administrator of National Banks**

Washington, DC 20219

No-Objection Letter #97-01

February 1997

12 U.S.C. 83

12 C.F.R. 7.2000

December 31, 1996

Cary Plotkin Kavy, Esquire
Cox & Smith
112 East Pecan Street
Suite 1800
San Antonio, Texas 78205-1521

Dear Ms. Kavy:

This responds to your request that the OCC not object to the proposal of First Victoria National Bank, Victoria, Texas ("Bank") to adopt a Rights Plan. You stated that, in accordance with 12 C.F.R. § 7.2000, the Bank has designated in its bylaws that Texas law has been selected for its corporate governance procedures. You also stated that the Rights Plan is permitted under Texas law and is not inconsistent with Federal banking statutes and regulations. Based on the information and representations provided, the OCC does not object to the Bank's proposal to adopt the Rights Plan.

The Rights Plan

You stated that the intended purpose of the Rights Plan is to enhance the ability of the board of directors of the Bank to protect shareholders against unsolicited takeover attempts that do not offer an adequate price to all shareholders or are otherwise not in the best interests of the Bank and its shareholders. The Rights Plan would not eliminate the possibility of a takeover attempt, but it would strongly encourage bidders to negotiate with the board of directors of the Bank.

The Bank has 5,000,000 shares of common stock, \$2.50 par value per share, authorized and 2,372,792 shares of common stock issued and outstanding. The common stock of the Bank is registered pursuant to Section 12(g) of the Securities Exchange Act of 1934 ("Exchange Act") and traded in the National Market System of NASDAQ.

Under the Rights Plan, the Bank would issue Rights to its shareholders as a pro rata dividend. Each shareholder of the Bank would receive the Right to purchase (at a below market rate) approximately one-half of a share of Bank common stock for each share of Bank common

stock owned if certain triggering events occur.¹ However, the board may choose to exchange the Rights for shares of common stock instead of permitting the shareholders to exercise their Rights to purchase common stock. The Rights Plan will provide that if a triggering event occurs, the board of directors may exchange the Rights for common stock at an exchange ratio of approximately one-half of a share of common stock of the Bank per Right.

The Rights Agreement also will provide that, until the occurrence of a triggering event, the Rights will be transferred with the shares of common stock of the Bank and the registered holders of the common stock will be deemed to be the registered holders of the Rights. As soon as possible following a triggering event, separate certificates evidencing the Rights will be mailed to the holders of record of shares of common stock of the Bank. Thereafter, the Rights will be transferable separately from the common stock of the Bank.

The triggering events under the Rights Plan would be (i) a tender offer or exchange offer that would result in beneficial ownership by a party of 20% or more of the outstanding common stock of the Bank; (ii) a merger or consolidation of the Bank; or (iii) the accumulation of 20% or more of the Bank's common stock by a party. However, none of these events would be a triggering event if the transaction is approved by the board of directors of the Bank. If a triggering event occurs, the party causing the triggering event would not be entitled to exercise its Rights to acquire additional shares of the Bank or to receive Bank common stock in exchange for its Rights.

Prior to the occurrence of a triggering event and for ten days thereafter, the board of directors of the Bank will be able to redeem the Rights for nominal consideration (approximately \$.01 per Right). If the board of directors redeems the Rights, it will redeem the Rights of all shareholders, including the shareholder that caused the triggering event. The redemption will be prohibited if the redemption payment would cause the Bank to be undercapitalized.

The terms of the Rights will be set forth in a Rights Agreement between the Bank and a Rights Agent. The Rights will remain in existence for ten years, unless redeemed, exchanged, or exercised prior to that time. The Rights will not entitle the holder to any shareholder rights, such as the right to vote or the right to receive dividends. The Rights Agreement will contain antidilution provisions to adjust the exercise price and the number of shares issuable pursuant to the Rights in the event of a stock dividend or the grant of additional rights or warrants to purchase shares of the Bank's common stock at a below market price. The Bank will not issue fractional shares upon the exercise of the Rights. In lieu of fractional shares, at the time the Rights are exercised, the Bank will pay cash equal to the same fraction of the current market price of one share of common stock of the Bank.

¹The exercise price of the Rights will be below the market price of the common stock but will be greater than the \$2.50 par value. The actual price will be determined with the assistance of a third party pricing expert prior to the adoption of the Rights Plan by the board of directors.

Permissibility of the Rights Plan

Under 12 C.F.R. § 7.2000, a national bank may elect to follow the corporate governance procedures of the law of the state in which the main office of the bank is located if those procedures are not inconsistent with applicable Federal banking statutes or regulations or bank safety or soundness. You represented that the Bank has designated in its bylaws that it has selected Texas, the law of the state in which the main office is located, for corporate governance procedures. You also represented that the Rights Plan is permitted under Texas law. In addition, you represented that the Rights Plan is not inconsistent with Federal banking statutes or regulations and is consistent with safe and sound banking practices.

We have not identified any aspects of the Rights Plan that are inconsistent with national banking laws. If the Bank redeems the Rights, the redemption appears not to conflict with 12 U.S.C. § 83. Section 83 provides that a bank generally cannot purchase its own stock. The purpose of the prohibition in section 83 is to prevent the impairment of bank capital. Dietrick v. Greaney, 309 U.S. 190, reh'g denied, 309 U.S. 697 (1940). The Bank's redemption of the Rights will not affect the Bank's permanent capital. Instead, the redemption will be treated comparably to a cash dividend. (See discussion of redemption of rights in Accounting Treatment below.) Therefore the redemption of the Rights is not a purchase of stock under section 83. Because the Bank will not be reducing the permanent capital of the Bank, the redemption of the Rights also is not a reduction of capital under 12 U.S.C. § 59.

The provision of the Rights Plan that provides that the Bank will issue cash in lieu of fractional shares is consistent with 12 C.F.R. § 7.2023. Section 7.2023 permits the Bank to pay to shareholders who would otherwise receive fractional shares the cash equivalent of those fractional shares.

In addition, the Rights Plan does not conflict with the prohibition in 12 U.S.C. § 1831o that a bank not make a capital distribution if after making the distribution it would be undercapitalized. The Rights Plan provides that the board of directors cannot redeem the Rights if the payment would cause the Bank to be undercapitalized.

Securities Filings Related to the Rights Plan

The Bank will issue a press release and file with the OCC a Current Report on Form 8-K reporting the adoption of the Rights Plan. See 12 C.F.R. § 11.2. The Bank will also file a Registration Statement on Form 8-A to register the Rights as a class of securities pursuant to section 12(g) of the Exchange Act. Id.

The Bank does not need to file a registration statement, under 12 C.F.R. § 16.3, for the securities underlying the Rights at the time it adopts the Rights Plan. However, the Bank must have that registration statement on file with the OCC at the time the Rights first become exercisable. See Div. Corp. Fin., No-Action Letter (January 7, 1987), "Registration of Rights

Issuable Pursuant to Stockholder Rights Plans,” [1987 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,411. In addition, the registration statement must be effective before any sales are made pursuant to the exercise of the Rights. Id.

In accordance with the SEC’s January 7, 1987 No-Action Letter on registration requirements for rights plans, the Bank has provided an opinion of counsel that states that the Rights Plan is permissible under Texas law and consistent with the directors’ fiduciary duties to the Bank and its shareholders. See Id.

Accounting Treatment

The Bank should account for the issuance of the Rights as a stock dividend. Upon issuing the Rights, the Bank should transfer the fair value, if any, of the Rights from undivided profits to a separate component of redeemable equity. We do not agree entirely with the statement on page five of your letter that “the issuance of the Rights will not affect the capitalization of the Bank.” While the total equity capital of the Bank will not change on the issuance of the Rights, specific components of book equity may change, affecting the computation of Tier 1 capital.

The fair value of the Rights at the date of issue is a question of fact to be determined by the Bank. Only if the Rights have no value, or such nominal value as to be clearly immaterial, will there be no change in equity components. In that event, the Bank need not make an accounting entry upon issuing the Rights.

If the board of directors exchanges the Rights for shares of common stock of the Bank, the Bank should apply the same accounting treatment that it would use if the board declared a stock dividend exceeding 20 to 25 percent of the Bank’s issued shares. In accordance with the Comptroller’s Manual for Corporate Activities, the Bank should transfer an amount equal to not less than the par value of the additional shares issued from undivided profits to a category of permanent capitalization (\$2.50 per share to common stock and the remaining amount to surplus).

If the Rights are exercised, the exercise price should be added to the capital stock account to the extent of par value, with any excess added to surplus. Any value of the Rights previously recorded as redeemable equity should also be transferred to surplus.

If the board of directors redeems the Rights, the Bank should charge the redemption first against the value of the Rights previously recorded as redeemable equity, and charge any excess against undivided profits. If redeemable equity exceeds the redemption price, the Bank should transfer the excess of redeemable equity to surplus. The redemption would not be considered a reduction in the permanent capital of the Bank for the purposes of 12 U.S.C. § 59, but any redemption in excess of redeemable equity may be subject to the dividend limitations in 12 U.S.C. §§ 56 and 60.

Conclusion

Based on the information and representations you have provided, the OCC does not object to the Bank's proposal to adopt the Rights Plan. In administering the Rights Plan, the Bank must comply with the requirements for changes in equity capital in 12 C.F.R. § 5.46. If you have additional questions, please call me at (202) 874-5210.

Very truly yours,

\s\

Elizabeth S. Malone
Senior Attorney
Securities and Corporate
Practices Division

ATTACHMENT - unavailable in electronic format