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Comptroller of the Currency  
Administrator of National Banks

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December 16, 2009

**Conditional Approval #940  
January 2010**

Gregory W. Gribben, Esq.  
Woods Oviatt Gilman LLP  
700 Crossroads Building  
2 State Street  
Rochester, NY 14614

Re: Savannah Bank National Association, Savannah, New York  
Charter Number: 12810  
Application for Reverse Stock Split  
CAIS Control Number: 2009 NE 12 343

Dear Mr. Gribben:

This responds to the Savannah Bank National Association, Savannah, New York (the “Bank”) application under 12 C.F.R. § 5.46 to elect the corporate governance provisions of New York law and complete a reverse stock split in accordance with those provisions. Based on the representations and commitments made by the Bank and its representatives, the application is hereby approved, subject to the conditions set forth below.

**I. Background**

**A. Facts**

The Bank is amending its bylaws to elect the corporate governance provisions of New York Business Corporate Law (“BCL”) to engage in a reverse stock split as permitted by New York law. The Bank proposes the reverse stock split to decrease the number of shareholders in order to qualify for subchapter S election. The Bank currently has 33 shareholders. Insiders own 90% of the common shares of the Bank, with the remaining shares held by a relatively small number of shareholders. Many of these shareholders are unresponsive to the Bank’s correspondence or have relocated without advising the Bank of their new mailing address. The Bank requires consent from all shareholders in order to qualify as a subchapter S corporation. Since the Bank is unable to contact some of these shareholders for their consent, the Bank will conduct a reverse stock split so that minority shareholders can redeem their shares.

The Bank proposes to conduct the reverse stock split as follows: the Bank will maintain the par value of its common stock at the current \$25.00 per share, therefore, at all stages of the reverse stock split, the par value of the common stock will remain under \$100 per share in compliance with 12 U.S.C. § 52. To effectuate the reverse stock split, the Bank proposes to reduce its 15,000 shares of common stock that are currently issued and outstanding, to 75 shares of common stock, with a par value of \$25.00 per share, in a 1-for-200 reverse stock split. Each shareholder who would otherwise hold a fractional share of common stock as a result of the reverse stock split will instead be entitled to receive a cash payment equal to \$250.00 per share of common stock held by such shareholder prior to the reverse stock split. Immediately following the reverse stock split, the bank will conduct a forward 200-for-1 stock split. Upon completion of the reverse and forward stock splits and the payment for fractional shares held by shareholders owning fewer than 1,039 shares prior to the reverse stock split, 13,961 shares of common stock will remain outstanding and 7 shareholders will own 100 percent of the common stock of the Bank. The amendments to the Bank's Articles of Association and the reverse and forward stock splits are subject to shareholder approval, which is anticipated to occur at a special meeting of shareholders duly called and held following the receipt of the Office of the Comptroller of the Currency's ("OCC") approval to conduct a reverse stock split.<sup>1</sup>

The 1-for-200 reverse stock split and the 200-for-1 forward stock split will reduce the Bank's capital stock account from \$375,000 to \$349,000 and the capital surplus account from \$625,000 to \$391,000. In the reverse and forward stock splits, par value of the common stock will remain the same at \$25.00 per share and the Bank will cash out fractional shares held by shareholders. Consequently, the Bank's capital will change only by the amount paid to cash out fractional shares (approximately \$260,000, assuming no shareholder exercises dissenters' rights), and the Bank's regulatory capital will remain in the "well-capitalized" category.

The Bank will provide dissenters rights as set forth in New York Business Corporate Law § 623. Directors will purchase qualifying shares in the Company to comply with 12 U.S.C. §72.

## **B. Corporate Governance**

National banks may adopt corporate governance procedures that comply with applicable federal banking law and safe and sound banking practices. OCC regulations provide that:

To the extent not inconsistent with applicable Federal banking statutes or regulations, or bank safety and soundness, 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*, the law of the state in which the holding company of the bank is incorporated, the Delaware General Corporation Law, Del. Code Ann. Tit. 8 (1991, as amended 1994, and as amended

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<sup>1</sup> Prior approval from the OCC is not required to conduct a forward stock split.

thereafter), or the Model Business Corporation Act (1984, as amended 1994, and as amended thereafter). A national bank shall designate in its bylaws the body of law selected for its corporate governance procedures.<sup>2</sup> [Emphasis added.]

The Bank's main office is located in Savannah, New York. The Bank may adopt New York corporate governance procedures to the extent that those procedures are not inconsistent with applicable Federal banking statutes or regulations. OCC regulations expressly permit a national bank to elect the corporate governance procedures of the state of the bank's main office of incorporation.<sup>3</sup>

The OCC has promulgated 12 C.F.R. § 7.2023 that codifies its decisions permitting reverse stock splits. The OCC confirms in the regulation the authority of national banks to conduct reverse stock splits where "the transaction serves a legitimate corporate purpose and provides adequate dissenting shareholders' rights."<sup>4</sup> The regulation specifically recognizes that reducing the number of shareholders in order to qualify as a subchapter S corporation is an example of a legitimate corporate purpose supporting a reverse stock split.<sup>5</sup> In the preamble to the rule, the OCC stated its intent was to recognize the flexibility that national banks have to restructure their ownership interests. The OCC also noted the consistency of its regulation with case law recognizing Congressional intent in the National Bank Act to simplify and encourage national bank consolidations.<sup>6</sup>

Counsel for the Bank represents that BCL § 802(b)(11)(amendments to change any outstanding shares into a different number of shares) and BCL § 802(b)(2) amendments to reduce stated capital authorizes New York corporations to effect reverse stock splits. New York law provides for dissenters' rights in connection with general corporate actions, including a reverse stock split.<sup>7</sup> In addition, the Bank certifies that the corporate procedures of BCL § 623 provide the shareholders with dissenters' rights that contain, at a minimum, the following elements:

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<sup>2</sup> 12 C.F.R. § 7.2000(b).

<sup>3</sup> See 12 C.F.R. § 7.2000.

<sup>4</sup> 12 C.F.R. § 7.2023(a).

<sup>5</sup> 12 C.F.R. § 7.2023(b)(1).

<sup>6</sup> OCC, Investment Securities; Rules, Policies and Procedures for Corporate Activities; Bank Activities and Operations (final rule), 64 Fed. Reg. 60092 (Nov. 4, 1999).

<sup>7</sup> BCL § 623 details procedures to enforce shareholder's rights to receive payment for shares. In addition, the OCC has previously approved a reverse stock split conducted under the corporate governance procedures of the State of New York. See Comptroller's Licensing Manual, "Capital and Dividends" at 12 (November 2007).

- Advance notice of dissenters' rights to shareholders before the shareholders' meeting at which the shareholders will vote upon the reverse stock split;
- An independent third-party appraisal of the shares of common stock if the Bank and any dissenting shareholders are unable to agree on the value of the dissenting shares;
- Payment by the Bank of the cost of appraising dissenting shares; and
- Binding arbitration by an independent third party, to be paid for by the Bank, if the court that would ordinarily hear an appraisal action under the corporate governance procedures refuses jurisdiction to appraise the shares of a national bank. Conduct of the arbitration will be consistent with the rules and procedures of the American Arbitration Association or other organization with expertise in alternative dispute resolution.

## **II. Discussion**

The Bank represents that reverse stock split transactions are permitted under New York law, and are consistent with applicable federal banking statutes or regulations. No provision of federal law expressly prohibits reverse stock splits. Several provisions of the National Bank Act authorize the elements of a reverse stock split and, when read together, allow a national bank to engage in a reverse stock split for a legitimate corporate purpose if the bank provides adequate dissenting shareholder rights.<sup>8</sup> Based on these authorities, the OCC has promulgated a regulation expressly permitting reverse stock splits if the transaction serves a legitimate corporate purpose and provides adequate dissenting shareholders' rights.<sup>9</sup>

The Bank will not reduce the par value of the Bank's shares. The Bank's permanent capital will be reduced only to the extent cash distributions will be remitted to those to whom fractional shares would otherwise be issued. See 12 C.F.R. § 5.67. Banks may amend their articles of association by the vote of a majority of the voting shares of stock to determine the number and par value of bank shares.<sup>10</sup> The National Bank Act permits a national bank to reduce its capital upon the vote of shareholders holding two-thirds of its capital stock and OCC approval.<sup>11</sup>

The Bank next proposes to replace each of the outstanding shares of common stock with new common stock at the rate of one share of new common stock for each 200 shares of common stock outstanding. The Bank will pay cash for the fractional shares outstanding. National banks have express authority to pay the cash equivalent of fractional shares of stock.<sup>12</sup> The cash

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<sup>8</sup> See *The Comptroller's Licensing Manual Booklet for Capital and Dividends* (November 2007) (Section on Reverse Stock Split); Conditional Approval 434 (Dec. 15, 2000); Interpretive Letter No. 786 (June 9, 1997); and Interpretive Letter No. 275 (Oct. 21, 1983).

<sup>9</sup> See 12 C.F.R. § 7.2023

<sup>10</sup> See 12 U.S.C. § 21a; see also 12 U.S.C. 52.

<sup>11</sup> See 12 U.S.C. § 59.

<sup>12</sup> See 12 C.F.R. § 5.67(c).

equivalent must be based on the market value of the stock or, if no market exists, a reliable and disinterested determination as to the fair market value of the stock.<sup>13</sup>

Judicial authority provides support for concluding that reverse stock splits for legitimate corporate purposes are consistent with the National Bank Act, where banks provide appropriate dissenters' rights. While the only Federal Court of Appeals case to address reverse stock splits directly, *Bloomington Nat'l Bank v. Telfer*, decided on the facts that the transaction before it violated the National Bank Act, the court declined to determine if reverse stock splits would be permissible for valid business purposes if dissenting shareholders' rights were provided.<sup>14</sup> The court also noted that the decision was limited to the facts of the case.<sup>15</sup>

In *NoDak Bancorporation v. Clarke*, the Eighth Circuit held that national banks could effect freeze-out mergers to allow a holding company to obtain 100 percent ownership so long as the national bank has a valid corporate purpose and observes dissenters' rights.<sup>16</sup> The *NoDak* court found that a national bank may engage in any merger not inconsistent with 12 U.S.C. 214a and 215-215a, and that freeze-out mergers are consistent with those sections.<sup>17</sup> More recently, a district court in the Tenth Circuit relied on *NoDak* to hold that a bank may effect a freeze-out merger to consolidate with another bank and become a wholly-owned subsidiary of an existing bank holding company.<sup>18</sup>

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<sup>13</sup> "The cash equivalent is based on the market value of the stock, if there is an established and active market in the national bank's stock." *Id.* In the absence of an established and active market in the Bank's stock, the Bank obtained an independent valuation as to the fair market value of its shares.

<sup>14</sup> *Bloomington Nat'l Bank v. Telfer*, 916 F.2d 1305 (7th Cir. 1990) ("*Bloomington*"). In *Bloomington*, the court concluded that the "reacquisition of capital stock, at a price significantly lower than the current stipulated value, combined with an avoidance of appraisal rights for the minority shareholders, is not in accordance with sections 83 [which at the time read that, "No association shall make any loan or discount on the security of the shares of its own capital stock, nor be the purchaser or holder of any such shares"] and 214a-215a of the National Banking Act." Pub. L. No. 106-569, Section 1207(a) rewrote the section to read, "No national bank shall make any loan or discount on the security of the shares of its own capital stock," thus eliminating the prohibition on national banks purchasing or holding their own stock. While the statutory provision dealt with by the *Bloomington* has been eliminated, assuming *arguendo* that the *Bloomington* court was correct in its interpretation of the statute as it existed at the time the court rendered its decision, it is noteworthy that the Bank will be affording dissenting shareholders appraisal rights, which should assure in any event, that the Bank will not be purchasing its shares at a discount, another concern of the *Bloomington* court.

<sup>15</sup> See *id.*, 916 F.2d at 1308 n.4, 1309.

<sup>16</sup> *NoDak Bancorporation v. Clarke*, 998 F.2d 1416 (8th Cir. 1993) ("*NoDak*").

<sup>17</sup> See *id.*, 998 F.2d at 1419-20 and 1425.

<sup>18</sup> See *Moody v. First National Bank, Sallisaw*, CY-00-306-5 (E.D.Ok. July 5, 2001).

In *Lewis v. Clark[e]*, the Eleventh Circuit determined that a national bank may not offer different consideration to shareholders when the bank effects a freeze-out merger under 12 U.S.C. § 215a.<sup>19</sup> The court held that the OCC lacked authority to approve mergers where minority shareholders receive cash for their shares and majority shareholders receive stock in the resulting bank, even in cases where the minority shareholders have appraisal rights. The *Lewis* case predated 12 C.F.R. Section 7.2023. Thus, that case did not involve a decision, like the present case, where a regulation expressly permits reverse stock splits. Since the OCC has adopted section 7.2023 following a notice and comment procedure, courts reviewing an OCC decision approving a reverse stock split should give deference to the OCC's reasonable interpretation of a statute that it administers.<sup>20</sup> Moreover, the OCC has permitted national banks to conduct reverse stock splits in numerous situations since *Lewis* and *Bloomington* were decided. In the period since *Lewis* and *Bloomington*, the OCC has approved reverse stock splits for banks located in seventeen states in cases where the banks had legitimate corporate purposes in conducting the transactions.<sup>21</sup> Thus, applicable statutory and regulatory provisions and the weight of judicial precedent would permit reverse stock splits for legitimate business purposes, provided dissenters' rights are available.

The Bank has articulated legitimate business purposes in effecting a reverse stock split. The Bank indicates it wants to decrease the number of shareholders to qualify for a subchapter S election. Eliminating burdens associated with a shareholder constituency is a proper business purpose.<sup>22</sup> The OCC expressly recognizes these corporate purposes in its regulation permitting national banks to conduct reverse stock splits.<sup>23</sup>

To avoid undermining the shareholder protections of 12 U.S.C. §§ 214a and 215-215a, however, a reverse stock split must provide shareholders adequate dissenters' rights to ensure that they receive a fair price for their shares.<sup>24</sup> Those dissenters' rights need not be identical to those located in sections 214a, 215, and 215a.<sup>25</sup> Accordingly, the Bank may effect a reverse stock split as long as it has a valid corporate purpose for the transaction and observes appropriate dissenters' rights.

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<sup>19</sup> *Lewis v. Clark[e]*, 911 F.2d 1558 (11th Cir. 1990), *reh 'g denied*, 972 F.2d 1351 (1991) ("*Lewis*")

<sup>20</sup> *NationsBank v. Variable Annuity Life Ins. Co.*, 513 U.S. 251 (1995); *United States v. Mead Corp*, 533 U.S. 218, 231 n. 13 (2001); *see also*, *National Cable & Telecommunications Association v. Brand X*, 545 U.S. 967 (2005).

<sup>21</sup> *See* Advisory Letter 2002-6, *supra*; Conditional Approval 541 (July 30 2002).

<sup>22</sup> *See Leader v. Hycor, Inc.*, 479 N.E.2d 173, 178 (Mass. 1985); *see also Nash v. Farmers New World Life*, 1976 U.S. Dist. 15,846, \*48 (S.D. Ohio, 1976).

<sup>23</sup> 12 C.F.R. § 7.2023(b).

<sup>24</sup> *NoDak Bancorporation v. Clarke*, 998 F.2d 1416 (8th Cir. 1993).

<sup>25</sup> *Id.*

The minority shareholders in the reverse stock split will receive dissenters' rights comparable to those under the National Bank Consolidation and Merger Act (the "NBCMA").<sup>26</sup> Specifically, the Bank has represented that it will provide notice of dissenters' rights to the minority interest holders before the shareholder meeting acting on the reverse stock split proposal; pay the cost of an independent third party appraisal of the shares if the Bank and any dissenting shareholders are unable to agree on the value of the dissenting shares; and pay the cost of a binding arbitration by an independent third party, if the court that would ordinarily hear an appraisal action under the corporate governance procedures refuses jurisdiction to appraise the shares of a national bank. The Bank will not pay the costs of attorneys' fees incurred by and costs of experts retained by dissenting shareholders for any such proceeding.

### **III. Conclusion**

For the above reasons, including the representations and commitments made by the Bank and its representatives, we find that the reverse stock split application is legally authorized and meets the other statutory criteria for approval. Accordingly, this application is hereby approved, subject to the following conditions:

1. The Bank will elect the corporate governance provisions of New York law.
2. The Bank will provide for dissenters' rights comparable to those found in 12 U.S.C. §§ 214a, 215, and 215a.
3. If any shareholders dissent from the reverse stock split, the Bank will pay the cost of any appraisal that may occur, but not the costs of attorneys' fees incurred by and costs of experts retained by dissenting shareholders.
4. If the appropriate court(s) decline to accept jurisdiction of an appraisal action, the Bank will pay for binding arbitration by an independent third party to appraise the stock but not the costs of attorneys' fees incurred by and costs of experts retained by dissenting shareholders.

The conditions of this approval are conditions "imposed in writing by a Federal banking agency in connection with any action on any application, notice, or other request" within the meaning of 12 U.S.C. § 1818. As such, the conditions are enforceable under 12 U.S.C. § 1818.

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<sup>26</sup> Under the NBCMA, a dissenting shareholder must either vote against the merger, or give written notice of dissent prior to or at the shareholder meeting at which the shareholders vote on the merger. The value of the dissenting shareholders' shares is determined by an appraisal made by a committee of three persons: one chosen by the dissenting shareholders, one chosen by the directors of the bank (as it exists after the merger), and one chosen by the other two members of the committee. If the committee fails to determine a value of the shares, or a dissenting shareholder is not satisfied with the value determined, the OCC must make an appraisal of the shares. See 12 U.S.C. §§ 214a(b), 215(b)-(d), and 215a(b)-(d).

Please notify the OCC when the change in capital has been completed in accordance with this approval. The notification should state the date of the change, and the dollar amount of the reduction in the common stock and surplus account associated with the payment for fractional shares. The notification should include a certification that shareholders approved the change in capital structure according to law, regulations, and the Bank's Articles of Association. A secretary's certificate of shareholder approval and a certified copy of the amendment to the Articles of Association should be included. The notification also should include a statement that the change in the capital structure complies with all applicable laws and regulations. Upon receipt of the notification, the OCC will review the reduction in capital attributable to the payment for fractional shares.

If the reverse stock split is not consummated within one year from the approval date, the approval shall automatically terminate unless the OCC grants an extension of the time period. Please advise Sandya Reddy, Senior Licensing Analyst, within 10 days of the effective date of the reverse stock split.

Please include CAIS Control Number 2009-NE-12-343 on all correspondence related to this application.

This conditional approval and the activities and communications by OCC employees in connection with the filing do not constitute a contract, express or implied, or any other obligation binding upon the OCC, the United States, any agency or entity of the United States, or any officer or employee of the United States, and do not affect the ability of the OCC to exercise its supervisory, regulatory and examination authorities under applicable law and regulations. Our preliminary conditional approval is based on the bank's representations, submissions, and information available to the OCC as of this date. The OCC may modify, suspend or rescind this approval if a material change in the information on which the OCC relied occurs prior to the date of the transaction to which this decision pertains. The foregoing may not be waived or modified by any employee or agent of the OCC or the United States

If you have any questions, please contact Sandya Reddy, Senior Licensing Analyst, at 212-790-4055.

Sincerely,

*signed*

J. Greg Parvin  
Director for District Licensing