The Lending Limit Exercise

prepared by

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&

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for use in connection with

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MEMORANDUM

To: Incoming Associate
From: Nancy I. Kimble
Re: Meridian National Bank Loan to Zenith Resorts Corporation
Date: October 20, 1998

Welcome to Hays and Brown.

Your first assignment is to draft an opinion letter as to the amount that Meridian National Bank may loan to Zenith Resorts Corporation. Meridian National Bank is a new client of the firm, and while this first matter is relatively simple, we hope to cultivate Meridian National Bank into a major client of the firm. Thus, I will appreciate your extra effort on this assignment.

I am forwarding to you the file on this loan in which you should find everything necessary to draft the opinion letter. As you will see when you review the attached materials, William Coleman, a former associate at this firm, has already done a considerable amount of research on this project. In the course of that research, William uncovered another Meridian loan, one to the Mile High Development Company, that may bear on your analysis. As a result of William’s research, John Nader has also asked us to include in our opinion a quick review of the Mile High loan, as originally underwritten. Accordingly, our opinion should be drafted to address both transactions. William has pulled together the relevant statutes, regulations and agency interpretations, which are appended to the attached file. Before he left, William mentioned to me that some of the statutes and regulations have been amended in past couple of years, so some of the cites in the agency interpretations do not match the current statutes or regulations.
However, the agency interpretations still represent the current positions of the agencies.

Since you probably have not worked on an opinion letter of this sort before, I am also sending along assorted background materials, including a few sample opinion letters from other areas of the law to give you an idea of how to draft the letter. Don’t spend too much time worrying about the content of those other letters. Instead, focus on drafting an opinion applying the federal banking laws and regulations to the facts detailed in the file.

The deadline on this project is, I’m afraid, fairly tight. We need to get a final opinion to Meridian’s Board of Directors by next Tuesday, October 27th, so they will be in a position to approve the transaction at their next meeting. Unfortunately, I will be out of town at the ABA convention in Honolulu for the entire week, and you won’t be able to reach me. Just do the best you can, and make sure you get your draft on my desk by 10:00 a.m. Tuesday morning.

Good luck.

enclosures

NIK/je
List of Enclosures

Letter from John H. Nader to Nancy Kimble (October 7, 1998)  
(balance sheet attached)

Memorandum from Walter H. Coleman to Nancy Kimble (October 16, 1998)

Letter from John H. Nader to Nancy Kimble (October 19, 1998)

Appendices:

I. Compilation of Statutory and Regulatory Sources
   A. 12 U.S.C.S. § 84 and Associated Regulations and Interpretations
      1. 12 U.S.C. § 84
      2. 12 C.F.R. Part 32
      4. OCC Int. Ltr. 400 (Nov. 9, 1987)
      5. OCC No. Obj. Ltr. 88-3 (March 29, 1988)
   B. 12 U.S.C.S. §§ 375a, 375b and Associated Regulations and Interpretation
      1. 12 U.S.C. § 375a
      2. 12 U.S.C. § 375b
      3. 12 C.F.R. Part 215 (“Reg O”)
      4. 12 C.F.R. Part 31
      5. OCC Int. Ltr. 166 (Oct. 8, 1980)
   C. 12 U.S.C.S. §§ 371c, 371c-1


III. Background Materials on Opinion Letters
   A. Stanley J. Friedman, “The Formal Opinion Letter,”

Ms. Nancy Kimble, Esq.
Hays & Brown, P.C.
Suite 2000
180 Greenwich Street
Meridian, Ames 55555

Dear Ms. Kimble:

As I mentioned during our telephone conversation of October 5, Meridian National Bank ("Meridian") is seeking a new law firm to represent the bank in connection with certain regulatory issues. You and your firm come highly recommended as federal banking law experts, and I look forward to working with you in the years ahead. As an initial matter, I am writing to request, on behalf of Meridian, a legal opinion from your firm as to the size of loan that Meridian may extend to Zenith Resorts Corporation ("Zenith") at this time.

Over the years, Meridian and Zenith have worked together on a number of real estate development projects. At the present time, Meridian’s relationship is limited to a relatively modest role in financing the firm’s construction of the Apex Hotel and Ski Resort. Meridian holds a $2 million participation in a syndicated loan to Zenith for that project. Meridian also has outstanding a $500,000 standby letter of credit issued on Zenith’s account in favor of Acme Window Corporation, a major supplier for the Apex Hotel. In addition, Meridian has a binding loan commitment to Zenith of $8 million for cost overruns, but Zenith has yet to make any draws on that commitment.

Recently, we have been looking to expand our relationship with Zenith, and it now appears that such an opportunity has presented itself in the form of Zenith’s newest project, the Crown Plaza, a hotel and retail complex to be located in downtown Meridian. Construction costs for the Crown Plaza are currently projected to be $45 million. Zenith’s management has indicated that they would prefer to obtain the bulk of their $45 million financing needs from a single lender. As I am sure you will appreciate, Meridian would very much like to serve as lead lender for this project. Our lending officers and in-house legal staff are currently working on a financing proposal for the project, along with the standard supporting loan documentation. Where we need your help is in obtaining a legal opinion for our board of directors regarding the amount that Meridian may legally loan to Zenith. (In response to some technical oversights uncovered in an OCC examination of Meridian several
years ago, the Board agreed to obtain this kind of outside opinion before committing to make substantial loans of the sort we envision for Zenith.) To ensure that we land this deal, we would like to offer Zenith financing for as close to the full $45 million as possible. We are not interested in selling a participation in the Crown Plaza loan to any other banks at this time. Thus, your opinion letter should reflect the size of loan that Meridian National Bank itself can take on.

As a starting point, I have enclosed the unaudited second quarter financial statement for Meridian. If you require any additional information about the project, please feel free to contact me or my staff here at Meridian.

Meridian wants very much to work with Zenith on the Crown Plaza. It is a high visibility project and Zenith is a very important developer. As the loan appears straightforward in all respects, we hope to finalize our financing proposal in the next few weeks. The Meridian Board of Directors is scheduled to review the transaction at its next meeting, which is scheduled for Wednesday, October 28th. We hope they will be able to approve the transaction at that meeting, so we need your opinion by that date, if not sooner.

Again, I look forward to working with you. Please call my office if I can be of any further assistance.

Sincerely,

John H. Nader

President
Meridian National Bank

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JHN/pam
# CONSOLIDATED STATEMENT OF CONDITION
(unaudited)

September 30, 1998

## ASSETS

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## LIABILITIES

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## CAPITAL ACCOUNTS

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<td><strong>TOTAL</strong></td>
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**SOURCE:**
As you and I have discussed, I am leaving Hays & Brown at the end of this week to take a position with the Securities and Exchange Commission. As such, I will be unable to complete the opinion letter requested by Meridian National Bank (the “Bank”). I have, however, done some preliminary investigations on the project. The results of my fact finding to date are detailed below.

According to my review of various public documents in our library, the Bank is a national bank serving Meridian, Ames and the surrounding community. It was established by the Forster family back in the 1920's, and the family retained control of the bank until 1980. At that time, the Forsters formed a bank holding company, Meridian Bancorp, Inc. (an Ames corporation) which acquired all of the bank’s shares. Most of the shares of the holding company were sold to the public. The holding company has three wholly-owned subsidiaries: the Bank, Meridian Mortgage Company, Inc. (an Ames corporation), and Meridian Community Development Corporation (an Ames corporation).

George Forster, the Chairman of the Board of the Bank and grandson of one of the Bank’s founders, holds the largest single block of the holding company’s stock, which represents 9.5 percent of the stock outstanding. Three other directors are also related to the Forster family in one way or another and possess significant indirect investments in the Bank, each holding 7 percent of the
outstanding stock of the holding company. (Aside from George Forster, the only Forster-family director employed at the Bank is John Nader, George Forster’s brother-in-law, who now serves as President of the Bank. The other Forster directors are distant cousins and do not hold management positions.) The other seven members of the Bank’s board of directors are unrelated members of the business community who have been invited to join the board over the years. These other directors have only nominal holdings of holding company stock.

I visited the Bank earlier this week. While there I examined correspondence of the loan committee and spoke to Leon Harris and Janice White, officers on the Bank’s loan committee. The correspondence and interviews with members of the loan committee confirmed the details of John Nader’s October 7, 1998, letter as follows:

- Zenith Resorts Corporation ("Zenith") is currently seeking an acquisition, development and construction (ADC) loan for a hotel/retail complex in downtown Meridian. It is anticipated that ADC costs will approximate $45 million. The ADC loan is to be evidenced by a promissory note executed by Zenith. The note is to be secured by a first lien construction deed of trust, an assignment of rents, and a security agreement on the real property together with all improvements to be constructed thereon. The Bank wishes to commit to the maximum ADC loan possible to Zenith.

- The Bank has outstanding a $500,000 standby letter of credit issued on the account of Zenith in favor of Acme Window Company.

- The Bank has a $2 million participation in a loan to Zenith that is secured by a second mortgage of the Apex hotel property.

- The Bank has an $8 million loan commitment to Zenith, which is yet to be drawn upon.¹

In the course of my conversations with Janice White, there was some confusion as to the relationship between the Crown Plaza

¹ Leon Harris indicated that Zenith does not want to draw down its $8 million loan commitment with this loan, but instead desires a loan separate from the loan commitment.
transaction and a $12 million working capital loan that the Bank made several months ago to a limited partnership, the Mile High Construction and Development Company, Ltd., ("Mile High") to finance payroll and over-head for a Mile High vacation homes development called Pine Mountain Retreat ("Pine Mountain"). That loan was secured by a second mortgage on the Pine Mountain property. Last month, the Bank lent Mile High an additional $500,000 to finance some engineering and landscaping work to stabilize a portion of the Pine Mountain west slope which had been damaged by a massive mudslide.

At first, Janice indicated that the Mile High loan was part of the Crown Plaza project. But after reviewing her notes and consulting with Leon, she told me that Mile High and Zenith simply have had a long-standing business relationship. Mile High works predominantly on Zenith construction projects, deriving 65 percent of its income from Zenith projects. The other 35 percent of Mile High’s income is generated by non-Zenith construction projects, such as the Pine Mountain project, and various other real estate related transactions. The reason that Janice confused the two projects is that the land on which Zenith proposes to construct the Crown Plaza project is to be acquired from Mile High for approximately $10 million. (A qualified independent appraiser has certified that $10 million is the fair market value of the property if developed as Zenith proposes.)

At my request, Leon Harris showed me the Bank’s due diligence file on the Mile High loan. In that file, Leon found a list of Mile High limited partners as well as a copy of the limited partnership agreement. The partnership was organized under the Revised Uniform Limited Partnership Act (1976) with the 1985 Amendments (RULPA (1985)), which the state of Ames adopted several years ago. The only name of note in the list of partners was that of George Forster (the Bank’s Chairman), who was one of ten limited partners listed. According to bank records, Mr. Forster and each of the other nine limited partners holds a 6 percent interest in Mile High while the general partner (a local businessman named Skip O’Toole) holds the remaining 40 percent interest. According to the partnership agreement, the Mile High limited partners are free to vote on a variety of topics under the partnership agreement, but it is not clear from the loan file the extent to which Mr. Forster and the other limited partners have exercised this power at Mile High.²

² Under the version of RULPA adopted in Ames, the partnership is not required to make public disclosure of financial information or internal operations. (I have attached an excerpt from a treatise on partnership explaining how the RULPA works). Leon Harris was concerned that we not make any
According to the Bank’s records, however, Mr. Forster appears not to have participated in the Bank’s decision to make the Mile High loan or the Board’s approval of that transaction.

Aside from a few loose ends regarding the Mile High loan, I believe that we will be in a position to prepare an opinion letter concerning the Bank’s proposed loan to Zenith. I have collected all of the federal banking statutes and regulations (along with a couple of interpretive releases) which establish lending limits for national banks, and have attached them to this memorandum. (It is not clear to me that all of these materials are relevant to the transaction we have been asked to review, but I thought it would be helpful to pull everything together in one place.) Unfortunately, I have not had the chance to apply the regulations to the facts outlined above, so I leave that task to my replacement.

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WHC/je
Ms. Nancy Kimble, Esq.
Hays & Brown, P.C.
Suite 2000
180 Greenwich Street
Meridian, Ames 55555

Dear Ms. Kimble:

While I was out of the office last week, I received a call from a William Coleman of your firm regarding George Forster and Mile High Construction and Development Company, Ltd. I am writing in response to several questions Mr. Coleman left with my assistant.

To the best of my recollection, I had not previously been aware of George’s interest in Mile High, and don’t recall that fact coming up when we make the loan earlier this year. Frankly, I’m not surprised. George has financial interests in many different real estate deals in the region, and his interest in Mile High is pretty small (at least by his standards). In any event, I have reviewed my notes on the transaction, and it appears that George was not directly involved in the Mile High loan and did not even attend the board of directors meeting at which the Board approved the transaction.

As your Mr. Coleman requested in the message he left with my assistant, I spoke with George about the Mile High partnership this morning. He indicated that he initially became involved in Mile High back in 1992 when Skip O’Toole, an acquaintance from the Hunting Valley Hunt Club, invited George, as well as 5 other club members, to join the partnership in 1992. (As you probably know, Hunting Valley is a private club with a large wildlife preserve in the mountains west of the city. Many members of the Meridian business community, including several other Meridian directors, are also club members but none of the other directors has any interest in Mile High.) In terms of Mile High operations, George has assured me that while he has voting rights under the partnership agreement, he and the other limited partners have remained entirely passive investors, and that Skip O’Toole, the general partner, manages all aspects of the partnership’s day-to-day operations. George has been so impressed by Skip’s business acumen that he put him on the board of directors of Meridian Community Development Corporation.
As we discussed the matter, George and I both came to the conclusion that from the Bank’s perspective, Zenith is a much more important potential client than Mile High ever will be. If necessary, George believes that it would be possible to move some or all of the Bank’s Mile High loan to another bank in Meridian. In fact, George tells me that Meridian State Bank and Trust Company has been actively soliciting Mile High business for some time now, and would probably be willing to purchase our Mile High loan on short notice. Of course, all things being equal, we’d prefer to keep the Mile High loan too. But, if we have to, we could move all or part of the loan over to Meridian State.

I hope this additional information is responsive to your needs. Mr. Coleman’s message did not indicate how the Mile High loan relates to our proposed transaction with Zenith, but I trust you will factor the transaction into your analysis as you see fit. Moreover, now that you have called our attention to George’s interest in Mile High, George and I would both feel better if you would expand your opinion to make at least a cursory review of that transaction and either confirm our understanding that Mile High loan was also consistent with applicable federal lending limits or advise us as to what corrective measures we should take at this time.

Thank you again for your assistance in this matter, and I look forward to receiving your opinion as soon as possible. Our next Board meeting is still scheduled for the 28th of October, and the Zenith loan is on the top of the agenda.

Sincerely,

John H. Nader
President
Meridian National Bank

JHN/pam