Comptroller of the Currency
Administrator of National Banks

Central District Office
One Financial Place, Suite 2700
440 South LaSalle Street
Chicago, Illinois 60605

Conditional Approval #709
November 2005

October 25, 2005

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Re: Application to Merge The First National Bank of Fremont into American Heritage Banco, Inc. (OCC Application Control Number: 2005-WO-12-0017) and,

Application by The First National Bank of Fremont for a fundamental change in its asset composition. (OCC Application Control Number: 2005-WO-12-0018)

Dear Messrs. St. Louis and Barnes:

This is to inform you that, as of the date of this letter, the Office of the Comptroller of the Currency (OCC) approved the application by The First National Bank of Fremont (Fremont) Fremont, Indiana, (Charter Number 10718) to merge into its nonbank affiliate, American Heritage Banco, Inc. (AHBI), under 12 U.S.C. § 215a-3 and 12 C.F.R. § 5.33(g)(5). The OCC also did not object the sale of all the deposit liabilities and substantially all the assets of The First National Bank of Fremont to Farmers State Bank (Farmers) under 12 C.F.R. § 5.53.

I. BACKGROUND

On September 6, 2005, Fremont applied to the Office of the Comptroller of the Currency ("OCC") for approval for a fundamental change in its asset composition under 12 C.F.R. § 5.53. Fremont is an insured national bank. The fundamental change in Fremont's asset composition will occur as a result of Fremont's agreement to sell substantially all of its liabilities and substantially all of its operating assets to Farmers State Bank, LaGrange, Indiana (Farmers), an insured state commercial bank, in a purchase and assumption transaction (Transaction). It is

planned that immediately after the Transaction, the insured status of Fremont will be terminated under 12 U.S.C. § 1818(q).[1]

On August 27, 2004, Fremont also applied to the OCC for approval for Fremont to merge into (AHBI), after the consummation of the Transaction and the termination of Fremont's status as an insured bank (the merger). AHBI is the immediate parent, and the sole shareholder, of Fremont.[2] It is not a bank, and so it is a nonbank affiliate of Fremont. AHBI is organized as an Indiana corporation. Its principal place of business is in San Jose, Illinois. Fremont plans to consummate the merger immediately after the consummation of the Transaction and the termination of Fremont's status as an insured bank. Fremont hopes to consummate the merger on the same day as the Transaction, but in any event it will complete the merger as soon as possible thereafter. As a result of the merger, Fremont's separate existence as a national bank will end, and its charter will be terminated.

II. DISCUSSION

A. The Fundamental Change in Asset Composition

Fremont applied to the OCC for prior approval of a fundamental change in its asset composition under 12 C.F.R. § 5.53.[3] Under section 5.53(c)(1)(i), a national bank must obtain prior written approval of the OCC before changing the composition of all, or substantially all of its assets through sales or other dispositions. In the Transaction, Fremont will sell all its deposits and

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[1] Under section 1818(q), whenever the liabilities of an insured depository institution are assumed by another insured depository institution, the insured status of the institution whose liabilities are assumed "shall terminate on the receipt by the Corporation of satisfactory evidence of such assumption . . . . " 12 U.S.C. § 1818(q). The Federal Deposit Insurance Corporation ("FDIC") requires the assuming institution to certify to the FDIC that it has assumed the deposit liabilities and considers such certification satisfactory evidence. 12 C.F.R. § 307.1. On October 6, 2005, the FDIC confirmed that the insurance termination order would be prepared and ready for issuance after certification of the assumption of deposit liabilities.

[2] Management of Fremont has been unable to locate a stock ledger or other evidence in its records confirming AHBI's ownership of all of Fremont's stock. Under prior management, Fremont converted to a bank-bank holding company structure, at which time Fremont believes that all of its stock was acquired by AHBI. Fremont represents that it has undertaken a diligent search for its stock ledger or other evidence of stock ownership, and Fremont has not identified any evidence, which would cause it to believe that AHBI is not its sole shareholder.

[3] The OCC recently issued 12 C.F.R. § 5.53, and it became effective on October 1, 2004. *See* 69 Fed. Reg. 50293 (August 16, 2004).

substantially all of its operating assets. Thus, it is clearly within the scope of section 5.53(c)(1)(i). The principal purpose of adopting 12 C.F.R. § 5.53 was to address supervisory concerns raised by so called "dormant" bank charters by providing the OCC with regulatory oversight and a means to monitor them.

In the case of Fremont, Fremont plans to merge into its nonbank affiliate parent immediately after the Transaction that would make Fremont a "dormant" charter. Thus, OCC concerns over the continuation of "dormant" charters are addressed. OCC approval of Fremont's application would be consistent with the language and purpose of section 5.53. This approval is therefore granted in part based on the representation that the merger will occur immediately after the Transaction, or as soon as possible thereafter, and to require Fremont to contact the OCC immediately if the merger does not occur on or before November 3, 2005.

B. The Merger

In the merger, Fremont will be merged into AHBI, an Indiana corporation. After the merger, AHBI will be the surviving entity, and the bank will cease to exist. The merger is authorized under 12 U.S.C. § 215a-3.

Section 215a-3 authorizes a national bank to merge with a nonbank subsidiary or affiliate: "Upon the approval of the Comptroller, a national bank may merge with one or more of its nonbank subsidiaries or affiliates."[4] The statute does not limit its scope to mergers in which the national bank is the surviving entity, and so a merger into a nonbank affiliate is within its scope. Moreover, in the OCC's implementing regulations (quoted below), the OCC has expressly taken the position that mergers into a nonbank affiliate are covered. However, the regulation limits these transactions to mergers involving a national bank that is not an insured bank.

The OCC regulations implementing 12 U.S.C. § 215a-3 set forth substantive and procedural requirements for the merger of an uninsured national bank with its nonbank affiliate in which the nonbank affiliate is the resulting entity. In particular, the regulation provides:

[4] 12 U.S.C. § 215a-3(a), as added by section 1206 of the Financial Regulatory Relief and Economic Efficiency Act of 2000 (Title XII of the American Homeownership and Economic Opportunity Act of 2000), Pub. L. No. 106-569, 114 Stat. 2944, 3034 (December 27, 2000). Section 1206 was adopted in order to facilitate the ability of banking organizations to effect corporate restructuring between national banks and their subsidiaries and affiliates in the most efficient way possible, while preserving regulatory oversight by requiring OCC approval. *See* S. Rep. No. 106-11, 106th Cong., 1st Sess. 8 (1999).

> "With the approval of the OCC, a national bank that is not an insured bank as defined in 12 U.S.C. 1813(h) may merge with one or more of its nonbank affiliates, with the nonbank affiliate as the resulting entity, in accordance with the provisions of this paragraph, provided that the law of the state or other jurisdiction under which the nonbank affiliate is organized allows the nonbank affiliate to engage in such mergers. In determining whether to approve the merger, the OCC shall consider the purpose of the transaction, its impact on the safety and soundness of the bank, and any effect on the bank's customers, and may deny the merger if it would have a negative effect in any such respect."

Section 12 C.F.R. § 5.33(g)(5)(i) of the regulation imposes additional requirements that: (1) the bank comply with the procedures of 12 U.S.C. § 214a as if it were merging into a state bank, (2) the nonbank affiliate follow the procedures for mergers of the law of its state of organization, and (3) shareholders of the national bank who dissent from the merger have the dissenters' rights set out in 12 U.S.C. § 214a, note 12 C.F.R. § 5.33(g)(5)(ii)-(v) for additional information.

The proposed merger is covered by, and meets the requirements of, 12 U.S.C. § 215a-3 and 12 C.F.R. § 5.33(g)(5). First, as discussed above, Fremont's status as an insured bank will be terminated after the Transaction, so that at the time of the merger, Fremont will not be an insured bank. AHBI is a nonbank affiliate since it is not a bank and it is the sole shareholder of Fremont, note 12 C.F.R. § 5.33(d)(5) & 5.33(d)(8) for the definitions of control and nonbank affiliate.

Second, the law under which AHBI is organized allows it to merge with Fremont. AHBI is an Indiana corporation. Indiana permits its domestic corporations to merge with any "other business entities" formed, organized, or incorporated under the laws of Indiana or any other state, or the United States, provided certain statutory requirements are satisfied, note Ind. Code § 23-1-40-8(a) and (c). Indiana also has a special procedure for mergers between a parent corporation and a corporation that is at least 90% owned by the parent corporation, note Ind. Code § 23-1-40-4. Therefore, the merger is permitted under Indiana law.

Third, Fremont is complying with the procedures of 12 U.S.C. § 214a to the extent applicable. Section 214a requires approval of the plan of merger by a majority of the board, notice to shareholders of the shareholders' meeting to vote on the merger by newspaper publication (unless waived by all shareholders) and by actual notice by mail (unless waived specifically by any shareholder), and approval by a vote of at least two-thirds of each class of stock. The application contains certified copies of the board of directors resolution approving the merger and the shareholder resolution approving the merger and waiving notice of the shareholder meeting by publication and by mail.

Fourth, AHBI is complying with the procedures for mergers by Indiana corporations. Indiana requires procedural steps similar to section 214a's outlined above. The application contains certified copies of the board of director's resolution approving the merger and the shareholder resolution approving the merger and waiving notice of the shareholder meeting by publication and by mail. AHBI will file the Articles of Merger with the Indiana Secretary of State following the closing of the Transaction, the receipt of OCC approval, and the issuance of the FDIC termination order.

Fifth, because Fremont is wholly owned by AHBI, there will be no dissenting shareholders, and so no issues relating to dissenters' rights are present.

Sixth, under the OCC's regulations, in reviewing mergers under section 215a-3, the OCC considers the purpose of the transaction, its impact on the safety and soundness of the bank, and any effect on the bank's customers, and may deny the merger if it would have a negative effect in any such respect. Provided the appropriate OCC units consider these factors and determine they do not require the merger be denied, this element in 12 C.F.R. § 5.33(g)(5) will be satisfied. In this regard, it should be noted that after the Transaction, Fremont, having sold substantially all its business to Farmers, would no longer be an operating company. The merger is simply a means to terminate the national bank charter. AHBI will continue with the remaining assets and liabilities, including contingent liabilities, of Fremont. Moreover, Earl McNaughton, the majority shareholder of AHBI, acknowledged AHBI's obligation to satisfy such liabilities and represented that assets would remain in AHBI for a sufficient period of time to satisfy these liabilities.

In addition, the proposed merger is not subject to sections 23A and 23B of the Federal Reserve Act, 12 U.S.C. §§ 371c & 371c-1. Under Regulation W, the merger of an affiliate into a bank is considered the purchase of an asset, and so a covered transaction, if the bank pays consideration or if there are liabilities in the affiliate that become liabilities of the bank, note 12 C.F.R. § 223.3(dd) for the definition of "purchase of an asset". The same rationale could be used to treat the merger of the bank into a nonbank affiliate as a sale of an asset under 12 U.S.C. § 371c-1. However, Regulation W does not address this point, and we believe it is an implausible interpretation of the statute for it to apply to a merger transaction that ends the bank's existence. First, there is no bank to be in violation of the statute or to be protected by it. Second, there is no transaction with the bank to which to apply the statutory standard (the transaction must be on terms and conditions at least as favorable to the bank as those in comparable transactions with unaffiliated parties).

III. CONCLUSION

The request for approval for a fundamental change in asset composition may be approved under 12 C.F.R. § 5.53. The proposed merger is legally permissible under 12 U.S.C. § 215a-3. In particular, the approval is based on Fremont's representation that the merger will occur shortly after the Transaction and the termination of Fremont's status as an insured bank. The application meets the various elements and legal requirements of the statute and 12 C.F.R. § 5.33(g)(5). The OCC may approve it, provided the appropriate OCC units consider the purpose of the transaction, its impact on the safety and soundness of the bank, and any effect on the bank's customers.

These approvals are subject to the following condition:

> If the merger does not occur within five (5) days after the Transaction, Fremont shall immediately notify the OCC and submit a plan to wind up its affairs and terminate its status as a national bank.

This condition of approval is a "condition imposed in writing by the agency in connection with the granting of any application or other request" within the meaning of 12 U.S.C. § 1818. As such, the condition is enforceable under 12 U.S.C. § 1818.

The OCC must be advised in writing in advance of the desired effective date for the merger so that the OCC may issue the certification letter for the merger. The OCC will issue a letter certifying consummation of the merger when we receive the following:

1. Written assurance from the Federal Deposit Insurance Corporation that Fremont is no longer insured.

2. Fremont's bank charter and any OCC documents in the possession of Fremont.

3. A copy of the final Certificate of merger filed with the Indiana Secretary of State.

This 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. The foregoing may not be waived or modified by any employee or agent of the OCC or the United States.

All correspondence and documents concerning this transaction should be directed to the undersigned at (312) 360-8863.

Very truly yours,

/s/

David Rogers
Director for District Licensing