

Personal Liability for Bank Directors Who Violate Lending Limit Statutes: Has Indiana Followed Congress' Lead?

MITCHEL MICK*

INTRODUCTION

Statutes limit the amount banks may lend to any single borrower.¹ A number of bank failures can be traced to losses resulting from loans made in violation of the bank's own lending policies or in violation of banking laws.² Regulatory agencies have the authority to take action

* J.D. Candidate, 1993, Indiana University School of Law—Indianapolis; B.S., 1987, Indiana University.

1. The Indiana lending limit statute provides in pertinent part that:

(a) The total loans and extensions of credit by a bank to a person outstanding at one (1) time and not fully secured, as determined in a manner consistent with subsection (b), by collateral having a market value at least equal to the amount of the loan or extension of credit may not exceed fifteen percent (15%) of the unimpaired capital and unimpaired surplus of the bank.

(b) The total loans and extensions of credit by a bank to a person outstanding at one (1) time and fully secured by readily marketable collateral having a market value, as determined by reliable and continuously available price quotations, at least equal to the amount of the funds outstanding may not exceed ten percent (10%) of the unimpaired capital and unimpaired surplus of the bank. The limitation in this subsection is separate from and in addition to the limitation contained in subsection (a).

IND. CODE § 28-1-13-1.5 (Supp. 1992).

The national legal lending limit as defined in the Garn-St. Germain Depository Institutions Act of 1982 provides (with some exceptions):

The total loans and extensions of credit by a national banking association to a person outstanding at one time and not fully secured . . . by collateral having a market value at least equal to the amount of the loan or extension of credit shall not exceed 15 per centum of the unimpaired capital and unimpaired surplus of the association.

12 U.S.C. § 84(a)(1) (1988).

2. A loan made in excess of the bank's legal lending limit is not itself an inherently risky loan. However, when combined with the accompanying failure to ensure adequate credit safeguards, the loan has the potential for disaster. A 1988 study conducted by the Office of the Comptroller of the Currency, analyzing 162 failures of federally chartered banks since 1979, found that 81% of these banks had non-existent or poorly followed loan policies; 59% had inadequate loan identification systems; and 69% had insufficient safeguards to ensure compliance with internal policies and banking laws. Stephen H. Collins, *National Bank Failures Studied in OCC Report*, 165 J. ACCT. 80 (1988). This OCC study predated Congress' effort to reform banking laws by its adoption of the

against directors who violate statutory lending limits.³

The Indiana banking statutes, like those of many other states, are analogous to the federal banking statutes in that they allow the regulatory agency to require the bank directors to "take affirmative action" to correct conditions resulting from a violation of applicable law.⁴ Some federal courts have denied federal regulatory agencies the authority to require reimbursement from directors under the "take affirmative action" clause, absent specific language authorizing reimbursement.⁵

Federal and state banking regulators also have the authority to assess civil monetary penalties against directors who violate their bank's legal lending limit. The assessment of penalties is a deterrent measure and does not compensate a bank for any resulting loss.

The parties who have standing to sue to require reimbursement from directors for losses occurring on a loan made in excess of the bank's lending limit, most commonly the shareholders or a party who lost money as a result of the violation, often do not know that a violation has occurred. The Indiana Department of Financial Institutions (DFI) may only disclose examination information to certain persons.⁶ Bank

Financial Institutions Reform, Recovery and Enforcement Act of 1989.

In 1991 alone, there were 123 bank failures. *Five More Bank Failures Raise 1991 National Total to 123*, BNA BANKING REP., Dec. 23, 1991, at 1046. It may forever be unknown how great a role the economy played in causing these recent failures in relation to the impact that mismanagement had on bringing about the failures. In any event, regulatory reforms at the national level must be given time to work and antiquated banking laws at the state levels must be brought up to date to avoid a great disparity between the powers of federal and state regulatory agencies.

3. State and federal statutes allow the assessment of civil monetary penalties, removal from office, orders to cease and desist from the violation, and requiring affirmative action to correct the conditions resulting from the violation. 12 U.S.C. §§ 93, 1818 (1988 & Supp. II 1990); IND. CODE § 28-11-4-7 (Supp. 1992); MO. ANN. STAT. § 361.261 (Vernon Supp. 1991); OHIO REV. CODE ANN. § 1125.08 (Anderson 1988); MICH. COMP. LAWS ANN. § 487.335 (West 1987).

4. IND. CODE § 28-11-4-7 (Supp. 1992); ILL. ANN. STAT. ch.17, para. 7311-1 (Smith-Hurd Supp. 1992); KY. REV. STAT. ANN. § 287.690 (Michie/Bobbs-Merrill 1988); MICH. COMP. LAWS ANN. § 487.335 (West 1987); MO. ANN. STAT. § 361.260 (Vernon Supp. 1992); OHIO REV. CODE ANN. § 1125.08 (Anderson 1988).

5. See, e.g., *Larimore v. Comptroller of Currency*, 789 F.2d 1244 (7th Cir. 1986).

6. The Indiana General Assembly has limited the persons to whom the DFI may provide examination information:

Except as otherwise provided, a member of the department or the director or deputy, assistant, or any other person having access to any such information may not disclose to any person, other than officially to the department, by the report made to it, or to the board of directors, partners, or owners, or in compliance with the order of a court, the names of the depositors or shareholders in any financial institution, or the amount of money on deposit therein at any

regulators conduct examinations on a regular schedule and have ready access to the information to detect violations. Limitations on disclosure of examination information effectively reduces the possibility that a party other than the DFI will obtain the information necessary to bring suit against the bank directors.

Requiring reimbursement from the bank directors before the bank has become insolvent is a prudent remedy that regulators should utilize more often. Replenishing the bank of funds lost through lending limit violations minimizes the snowball effect of a shrinking capital base initially caused by losses suffered from loans made in excess of the bank's legal lending limit. If the regulators must wait until the bank becomes insolvent before suing the bank directors, further harm results from the expense and delay in revoking the bank's charter.⁷

Not every bank director may have the funds to reimburse the bank for losses sustained on a loan made in excess of the legal limit. However, the potential of personal liability should provide more deterrence than the mere imposition of civil monetary penalties. In situations in which

time in favor of any depositor, or any other information concerning the affairs of any such financial institution.

IND. CODE § 28-1-2-30 (Supp. 1992). Further:

The director may disclose or make available to a:

- (1) state or federal law enforcement agency;
- (2) state or federal financial institution supervisory agency;
- (3) state or federal prosecutorial agency; or
- (4) private insurer of deposits accounts or share accounts of a financial institution; confidential information described under IC 28-1-2-30.

Id. § 28-11-3-3 (Supp. 1992)

7. Prior to 1966, the remedies available to federal regulators consisted of termination of the bank's deposit insurance or seizing control of the bank. Because these remedies were too drastic in many instances, Congress enacted 12 U.S.C. § 1818(b), allowing the issuance of cease and desist orders against banks. (This section was amended in 1978 to allow cease and desist orders to be issued against "any director, officer, employee, agent or other person participating in the affairs of such bank.") A senate report to the 1966 act, that the court in *Larimore v. Comptroller of Currency* found did not reveal legislative intent to allow the OCC to assess personal liability, states:

[I]t is essential that the federal supervisory agencies have the statutory and administrative facility to move quickly and effectively to require adherence to the law and cessation and correction of unsafe or improper practices Existing remedies have proven inadequate. On the one hand they may be too severe for many situations, such as taking custody of a institution or terminating its insured status. On the other hand they may be so time consuming and cumbersome that substantial injury occurs to the institution before remedial action is effective.

Larimore, 789 F.2d at 1250 (quoting S. REP. NO. 1482, 89th Cong., 2d Sess. (1966), reprinted in 1966 U.S.C.C.A.N. 3532, 3536-37).

the bank director does have the funds to reimburse the bank for losses resulting from lending limit violations, the bank will be able to recover from the adverse effects of the violation. In Indiana, a bank may not indemnify a director when the DFI imposes a civil monetary penalty against a director.⁸

A violation of the bank's legal lending limit and a failure of the directors to investigate excessive loans may indicate the directors committed intentional violations of applicable banking laws.⁹ When a lending limit violation occurs, the bank director may be liable for the full amount of the loan, not just the amount in excess of the lending limit.¹⁰ The bank director may be liable for large sums of money because a loan (or an aggregate of loans) made in excess of the bank's legal lending limit is typically a large loan.

This Note will analyze to what extent the DFI may bring suit in its own name against bank directors who have violated a bank's legal lending limit with the resulting loans causing a loss to the bank. Section I provides a brief overview of the banking regulatory system as it exists today. Section II analyzes the current statutory language in Indiana. Section III analyzes federal banking statutes that are analogous to the current Indiana banking statutes. Section IV analyzes other states' banking statutes that are analogous to the Indiana and federal banking statutes. Section V proposes that the DFI, before taking possession and appointing the Federal Deposit Insurance Corp. (FDIC) as receiver, be authorized to bring suit in its own name requesting reimbursement from bank directors who have violated lending limit statutes.

I. BACKGROUND OF THE BANKING REGULATORY SYSTEM

A bank may either be chartered by the state in which it is located or by the federal government. A bank chartered under federal law is a "national bank" and is under the supervision and examination of the Office of the Comptroller of the Currency (OCC).¹¹ A bank chartered under the laws of the state in which it is located is deemed a "state bank." State-chartered banks may be members of the Federal Reserve System (FRS), in which case they are subject to supervision and examination by the FRS and the state chartering authority.¹² State-chartered banks may also be insured by the Federal Deposit Insurance Corp.

8. IND. CODE § 28-11-4-9(c) (Supp. 1992). Currently, no statute exists which explicitly allows a bank to purchase and maintain insurance to cover civil monetary penalties assessed under Title 28.

9. *Cache Nat'l Bank v. Hinman*, 626 F. Supp. 1341, 1343 (D. Colo. 1986).

10. *See Corsicana Nat'l Bank v. Johnson*, 251 U.S. 68, 87 (1919).

11. P. Michael Davis & Rodney G. Alsup, *Kentucky Bank Directors Liability*, 11 N. KY. L. REV. 285, 285 (1984) (quoting EDWARD W. REED ET AL., *COMMERCIAL BANKING* (1976)).

12. *Id.*

(FDIC), in which case the regulators are the FDIC and the state chartering authority.¹³ If a state-chartered bank is a member of the FRS and the FDIC, the FRS is the designated federal regulator. State banks that are members of the FRS or insured by the FDIC are subject to state laws and regulations, as well as applicable federal laws.¹⁴

Each of these regulatory agencies has a somewhat different interest in enforcement. The FDIC, as an insurer of bank deposits, has a financial interest in the solvency of each insured bank. In regulating national banks, the OCC works to assure the safety and soundness of the banking system, although the OCC does not have the same financial interest as the FDIC because the OCC is not an insurer of bank deposits. State banking departments generally do not insure bank deposits. Therefore, a state banking department's interest in regulating banks, and the OCC's interest, are closely aligned. A state banking department's primary function is to ensure the soundness of the financial institution and the stability of the state's financial system.¹⁵

The regulatory agencies examine banks to ensure compliance with banking laws. Regulators assure adequate and proper financial services; protect the interests of depositors, borrowers, shareholders, and consumers; and promote the safety and soundness of financial institutions.¹⁶ Regulatory agencies should be given broad powers to carry out their duties to protect the public's interest.¹⁷

13. *Id.*

14. *Id.*

15. "The department is an agency of the state, vested with power to act for the protection of the interests of all parties, including the public." *Budnick v. Citizens Trust & Sav. Bank*, 44 N.E.2d 298, 302 (Ind. 1942).

Actually, the definition given of the function of the state banking department may determine the actions that the banking department may take as a means to its ends.

The dual banking system originated with the landmark case *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316 (1819). In today's dual banking system, with federal deposit insurance, some may argue that the primary function of state banking departments is to administer the chartering, branching, and mergers and acquisitions of banks. However, absent a wholesale discharge of the dual banking concept, state regulators retain the authority to fully regulate state chartered banks.

16. INDIANA DEP'T. OF FIN. INST., MISSION STATEMENT OF THE INDIANA DEPARTMENT OF FINANCIAL INSTITUTIONS (1987) (on file with author).

17. The Michigan Legislature has gone so far as to formalize its banking department's obligation to the public by enacting a statute indicating the department's goals. The statute provides in pertinent part:

It is the policy of this state that the business of all banking organizations shall be supervised and regulated in such manner as to insure the safe and sound conduct of such business, to conserve their assets and to eliminate unsound and destructive competition among such banking organizations and thus to maintain public confidence in such business and protect the public interest and the interests of depositors, creditors and shareholders.

MICH. COMP. LAWS ANN. § 487.302 (West 1987)

The OCC has specifically been given the authority to bring suit in its own name against directors in their individual capacities who violate federal banking laws.¹⁸ The other federal regulatory agencies have been given the authority to seek reimbursement from directors personally only by issuing a final order requesting such reimbursement.¹⁹ In Indiana, no reported cases exist wherein the DFI, before becoming a receiver, sought reimbursement from bank directors for losses on loans made in excess of the bank's legal lending limit.

II. INDIANA STATUTES MAY ALLOW THE DEPARTMENT OF FINANCIAL INSTITUTIONS TO REQUIRE REIMBURSEMENT FROM BANK DIRECTORS

In Indiana, no explicit statute exists, as exists for the OCC at the national level, which allows the DFI to sue directors in their individual capacities for losses resulting from loans made in excess of the bank's lending limit. If the courts liberally interpret the current Indiana banking statutes, the DFI may have the authority to request reimbursement before the bank is placed into receivership.²⁰

18. 12 U.S.C. § 93 (1988 & Supp. II 1990). See *infra* text accompanying note 47. The legislative history of this provision does not indicate why Congress would give the OCC standing to bring suit when the OCC does not have a financial interest in the viability of a financial institution.

The original bill that eventually became 12 U.S.C. § 93 contained the words "United States" in lieu of "Comptroller of the Currency". The congressional debate surrounding the insertion of "Comptroller of the Currency" was mostly concerned with avoiding a large number of similar actions being brought against a single bank in different jurisdictions. Congress wanted to consolidate the number of actions that could be brought against a financial institution by vesting such cause of action in the Comptroller of the Currency. CONG. GLOBE, 38th Cong., 1st Sess. 1889-90 (1864).

19. Congress has provided:

If, in the opinion of the appropriate Federal banking agency, any insured depository institution, depository institution which has insured deposits, or any institution-affiliated party is engaging or has engaged, or the agency has reasonable cause to believe that the depository institution or any institution-affiliated party is about to engage, in an unsafe or unsound practice in conducting the business of such depository institution, or is violating or has violated, or the agency has reasonable cause to believe that the depository institution or any institution-affiliated party is about to violate, a law, rule, or regulation, or any condition imposed in writing by the agency in connection with the granting of any application or other request by the depository institution or any written agreement entered into with the agency, the agency may issue and serve upon the depository institution or such party a notice of charges in respect thereof.

12 U.S.C. § 1818(b)(1) (Supp. II 1990).

20. The seriousness of bank failures and the importance of maintaining a financially sound financial system indicate that courts should be encouraged to broadly construe the DFI's authority.

In Indiana, only the DFI has the authority to issue a final order, and the DFI may seek enforcement of the order by applying to a "court having jurisdiction."²¹ A court may "stay, modify, or vacate a final order."²² A court may only alter a final order if the agency acted in a capricious or arbitrary manner, abused its discretion, or acted in excess of statutory authority.²³

The DFI may require bank directors to "take affirmative action to correct the conditions resulting from the practice or violation."²⁴ Requiring directors to provide reimbursement for losses sustained as a result of lending limit violations requires the directors to correct the condition resulting from the violation. Thus, the statute appears to allow a reimbursement order issued by the DFI. Shareholders may sue directors in their individual capacity for reimbursement. Therefore, the DFI, which by statute cannot disclose examination information to shareholders, should be allowed to bring suit. The Indiana banking statutes do not provide a definition for the appropriate remedies allowable under the "take affirmative action" clause, despite an analogous federal statute that does provide such a definition.

Because of the recent enactment of the "take affirmative action" clause in Indiana, no cases interpreting the clause have been reported, nor are there any cases in which the DFI has sought to bring suit against directors personally for lending limit violations. The "take affirmative action" clause does not appear to preclude a reimbursement action. Prior to the amendment of the federal banking statutes, some federal

21. IND. CODE § 28-11-4-10 (Supp. 1992).

22. *Id.* § 28-11-4-8(c).

23. Department of Fin. Inst. v. State Bank, 252 N.E.2d 248, 251 (Ind. 1969).

24. The amended language states:

(a) If upon the record made at a hearing under this chapter the department finds that the conditions specified in section 2 or 3 of this chapter have been established, the department may issue a final order.

(b) A final order must include separately stated findings of fact for all aspects of the order, including any remedy under subsection (c). Findings of ultimate fact must be accompanied by a concise statement of the underlying basic facts of record to support the findings.

(c) A final order may do any of the following:

(1) Require the financial institution and its directors, officers, employees, and agents to do any of the following:

(A) Cease and desist from the practice or violation.

(B) Take affirmative action to correct the conditions resulting from the practice or violation.

(2) Permanently remove a director or an officer.

(3) Impose a civil penalty not to exceed the amount specified in section 9 of this chapter. . . .

IND. CODE § 28-11-4-7(c)(1)(B) (Supp. 1992).

courts held that the federal regulatory agencies could not order reimbursement under federal statutes analogous to the current Indiana statute.²⁵

In the same bill providing the "take affirmative action" clause, the Indiana General Assembly gave the DFI the authority to assess civil monetary penalties against a director of a bank.²⁶ A penalty may be assessed when a bank director commits a violation of a statute, rule, or final cease and desist order and, either the "financial institution has suffered or will probably suffer substantial financial loss or other damage or, the interests of the financial institution's depositors could be seriously prejudiced by reason of the violation."²⁷ The General Assembly limited penalties to a maximum of \$15,000 per director for each violation.²⁸

Civil monetary penalties are punitive in nature and directed toward deterrence. The penalties do not compensate the injured party and do not alleviate the damage caused by violations of banking statutes. The amount collected in penalties goes to a state fund set aside for the

25. *Larimore v. Comptroller of Currency*, 789 F.2d 1244, 1256 (7th Cir. 1986). It should be noted that at the time *Larimore* was decided, 12 U.S.C. § 1818 did not contain a definition of what "affirmative action" was appropriate. Congress subsequently amended 12 U.S.C. § 1818 to provide a definition for "affirmative action". See *infra* note 60.

26. A final order issued by the DFI may "[i]mpose a civil penalty not to exceed the amount specified in section 9 of this chapter." IND. CODE § 28-11-4-7(c)(3) (Supp. 1992). See *infra* note 28.

27. The Indiana General Assembly has provided that:

If the director [of the DFI] determines that:

(1) a director or an officer of a financial institution has:

- (A) committed a violation of a statute, rule, or final cease and desist order;
- (B) engaged or participated in an unsafe or unsound practice in connection with the financial institution;
- (C) committed or engaged in an act, an omission, or a practice that constitutes a breach of fiduciary duty as director or officer; or
- (D) been charged in a complaint, an indictment, or an information with commission of or participation in a crime involving dishonesty or breach of trust that is punishable by imprisonment for a term exceeding one (1) year under federal law or the law of a state; and

(2) either:

- (A) the financial institution has suffered or will probably suffer substantial financial loss or other damage; or
- (B) the interests of the financial institution's depositors could be seriously prejudiced by reason of the violation, practice, or breach of fiduciary duty; the director may issue and serve upon the director or the officer a notice of charges of the practice, violation, or act.

IND. CODE § 28-11-4-3 (Supp. 1992).

28. "A civil penalty imposed on a director or an officer under section 7 of this chapter may not exceed fifteen thousand dollars (\$15,000.00) for each practice, violation, or act found to exist in the final order." *Id.* § 28-11-4-9(a).

operations of the DFI.²⁹ Once a director violates a bank's lending limit, it becomes clear that the deterrent effect of penalties has failed.

Although the director may ultimately be assessed a penalty, the bank may remain in a weakened condition. Shareholders may lack knowledge of any wrongdoing on the part of the bank directors and never pursue a valid reimbursement action. Because the bank is not relieved of the financial burden placed on it as a result of the lending limit violation, the assessment of penalties is inadequate as a sole response to such violations.

In Indiana, once a bank is financially unsound, the DFI may take possession of the bank and bring suit against a bank director.³⁰ When the DFI takes over an institution, the DFI gains all the powers that a trustee obtains in a similar situation.³¹ The receiver is given express authority to bring suit against directors in the name of the receiver for the enforcement of any right or claim that is vested in the financial institution or shareholders.³²

When the bank deteriorates to the point that the DFI must take possession of it, the DFI's interest in the bank is not as great as that of a federal deposit insurer. The DFI has failed to satisfy its goal of assuring the soundness of the financial institution and must then focus on mitigating the damages caused by the bank failure. Because at this stage the DFI's interest is not very great, the DFI, in all probability, would not wish to incur the costs of pursuing litigation against the failed institution's directors. The FDIC, as insurer, has a much greater interest in pursuing the action at this stage in the proceedings.

The DFI could issue a formal order requiring the bank to seek reimbursement from the directors as an alternative way to ensure that the directors remedy their wrongs.³³ The statutory language that allows

29. The Indiana statute provides in pertinent part: "Civil penalties shall be deposited in the fund." *Id.* § 28-11-4-9 (emphasis added). The fund is defined as "the financial institutions fund . . ." *Id.* § 28-1-1-4. The money in the fund is used to pay expenses and compensation incurred by the DFI. *Id.* § 28-11-2-9. It should be noted that the operating budget of the DFI is supported by assessments to state chartered banks and is not dependent upon tax dollars. *Id.* § 28-11-3-5.

30. "[T]he department may take possession of the business and property of any financial institution . . . whenever it appears to the department that the financial institution . . . [h]as violated any statute . . . and that continued control of its own affairs threatens injury to the public, the financial community, its depositors, or other creditors . . ." *Id.* § 28-1-3.1-2.

31. *Old First Nat'l Bank & Trust Co. v. Scheuman*, 13 N.E.2d 551, 561 (Ind. 1938).

32. IND. CODE § 28-1-3.1-15 (West 1988).

33. See Marcia J. Staff & Richard W. Staff, *Administrative Enforcement of Legal Lending Limits: National Bank Directors and the OCC's Tangled Web*, 106 BANKING L.J. 116, 126 (1989).

the DFI to require the bank to "take affirmative action" to correct conditions resulting from the violation of banking laws appears to contemplate an order to the bank to take such action. The DFI can require the bank to bring suit and accomplish indirectly what the DFI possibly could not do directly. However, should the bank fail in its suit, the additional litigation costs would add another financial burden to the already financially troubled bank. If the bank should be required to bring suit and then fail, the banking community will argue that bank regulation is inadequate and overly burdensome. Any additional regulation of the banking industry is certain to draw sharp criticism from the banking community.³⁴

As indicated above, the DFI may bring suit against bank directors in their individual capacities after the DFI becomes the named receiver of the bank. This procedure is too time-consuming, costly, and extreme to be an effective remedy to cure the effects of a lending limit violation. The DFI may also assess penalties against bank directors who violate the bank's lending limit. Penalties do not compensate the bank for any loss that the bank has suffered on a loan made in excess of the bank's lending limit and are, therefore, not appropriate as the only remedy the DFI may utilize when a director has violated a lending limit. The most likely avenue for the DFI to pursue in suing bank directors in their individual capacities is to utilize the "take affirmative action" clause of the Indiana banking statutes. The DFI may then seek reimbursement from directors by requiring them to "take affirmative action" to correct the condition resulting from the directors' violation of the bank's lending limit.

III. FEDERAL STATUTES ANALOGOUS TO THE INDIANA STATUTES AND FEDERAL CASES INTERPRETING THOSE FEDERAL STATUTES

The current Indiana statute providing authority to issue a cease and desist order contains language analogous to the federal statute in existence prior to the adoption of the Financial Institutions Reform, Recovery

34. One argument against allowing the DFI an additional cause of action against directors is that such an amendment will result in a scarcity of qualified bank directors. This argument is without merit because national bank directors have been exposed to reimbursement liability for lending limit violations since the National Bank Act of 1864 yet national banks do not appear to have had difficulty attracting qualified directors.

The nature of a lending limit violation would certainly bring itself to the attention of a director. Any loan or series of loans that approach a bank's legal lending limit are going to be of a sizable dollar amount. Directors, in the ordinary course of their duties, will be aware of large borrowers and increase the monitoring on such borrowers, not only to ensure that the amounts loaned do not exceed the bank's lending limit, but also as a matter of credit policy.

and Enforcement Act of 1989 (FIRREA). The conflicting interpretations of the "take affirmative action" clause of the federal statute by federal courts led Congress to define the appropriate "affirmative action" that bank regulators may require of bank directors.

The "take affirmative action" clause provides:

In the event . . . the agency shall find that any violation . . . specified in the notice of charges has been established, the agency may issue . . . an order to cease and desist from any such violation or practice. Such order may . . . require the depository institution or its institution-affiliated parties . . . to cease and desist from the same, and further, to take affirmative action to correct the conditions resulting from any such violation or practice.³⁵

At the federal level, prior to the 1989 adoption of FIRREA, two cases dominated the field in dealing with bank director liability.³⁶ The courts in these two cases took opposing views of the "take affirmative action" clause. The Ninth Circuit Court of Appeals, in *del Junco v. Conover*,³⁷ held that the OCC could request reimbursement from directors when a loan made in violation of the bank's legal lending limit resulted in a loss to the bank.³⁸

In *del Junco*, the court reasoned that the OCC had "broad discretion to fashion a remedy" under 12 U.S.C. § 1818(b)(1).³⁹ The court held that "deference is due to the Comptroller's interpretation of the law under which he operates."⁴⁰ Previously, in *Groos National Bank v. Comptroller of Currency*,⁴¹ the Fifth Circuit Court of Appeals held that "once the Comptroller finds a violation he may, within his allowable discretion, fashion relief in such a form as to prevent future abuses."⁴² The court in *del Junco* interpreted the *Groos* holding as indicating that

35. 12 U.S.C. § 1818 (b)(1) (Supp. II 1990). FIRREA made minor changes to this section. Prior to FIRREA, this section used "bank" instead of "depository institution", and "director, officer, employee, agent, or other person participating in the conduct of the affairs of such a bank" instead of "institution-affiliated party."

36. See *Larimore v. Comptroller of Currency*, 789 F.2d 1244 (7th Cir. 1986); *del Junco v. Conover*, 682 F.2d 1338 (9th Cir. 1982), *cert. denied*, 459 U.S. 1146 (1983).

37. 682 F.2d 1338 (9th Cir. 1982), *cert. denied*, 459 U.S. 1146 (1983).

38. *Id.* at 1344.

39. *Id.* at 1340.

40. *Id.* at 1344.

41. 573 F.2d 889 (5th Cir. 1978). The *Groos* case concerned a cease and desist order prohibiting loans that were being made in violation of an agreement between the OCC and the bank.

42. *Id.* at 897.

the Comptroller "has broad discretion to cure the *effect* of a violation."⁴³ In a 1990 opinion, after the adoption of FIRREA, the Ninth Circuit reaffirmed its *del Junco* decision.⁴⁴

The Seventh Circuit, in *Larimore v. Comptroller of Currency*,⁴⁵ held that the OCC could not require reimbursement from directors under 12 U.S.C. § 1818(b)(1), but had to bring suit in federal court under 12 U.S.C. § 93(a) in order to seek reimbursement.⁴⁶ In *Larimore*, the OCC tried to order bank directors to reimburse the bank for losses resulting from loans made in violation of the bank's legal lending limit. The language of 12 U.S.C. § 93(a) provides:

If the directors of any national banking association shall knowingly violate, or knowingly permit any of the officers, agents, or servants of the association to violate any of the provisions of this chapter, all the rights, privileges, and franchises of the association shall be thereby forfeited. Such violation shall, however, be determined and adjudged by a proper district or Territorial court of the United States in a suit brought for that purpose by the Comptroller of the Currency, in his own name, before the association shall be declared dissolved. And every director who participated in or assented to the same shall be held liable in his personal and individual capacity for all damages which the association, its shareholders, or any other person, shall have sustained in consequence of such violation.⁴⁷

43. 682 F.2d at 1340 (emphasis added). *But see* *Larimore v. Comptroller of Currency*, 789 F.2d 1244, 1251 (7th Cir. 1986). In *Larimore*, the court interpreted the legislative history of 12 U.S.C. § 1818 as indicating that the OCC can only take action to prevent further deterioration of a situation. However, the court cited legislative history that reads: "[c]orrectly used, . . . these new powers can effectively enhance the ability of the financial institution regulatory agencies to cure unsafe or unsound situations." 789 F.2d at 1251. The court was more concerned that Congress did not expressly provide that the OCC could impose personal liability on a bank director. *Id.*

44. *Hoffman v. Federal Deposit Ins. Corp.*, 912 F.2d 1172, 1175 (9th Cir. 1990).

45. 789 F.2d 1244 (7th Cir. 1986). Initially, a panel of the court affirmed the order of the OCC in *Larimore v. Conover*, 775 F.2d 890 (7th Cir. 1985). Although affirming the OCC's order, "[the] . . . panel failed to address the initial issue of whether the Comptroller, pursuant to § 1818(b)(1), had the authority to order the directors to indemnify the bank for potential losses arising from their approval of loans in excess of the statutory limit contained in 12 U.S.C. § 84." *Larimore v. Comptroller of Currency*, 789 F.2d at 1248.

46. 789 F.2d at 1256.

47. 12 U.S.C. § 93(a) (1988). The OCC can bring a separate action against the bank directors without bringing suit to declare the dissolution of the bank. In an early opinion, interpreting what is now 12 U.S.C. § 93(a), the Eighth Circuit stated:

It can scarcely be supposed that congress intended to frame a law which in a

Under 12 U.S.C. § 93(a), the OCC must bring suit in a federal court when ordering reimbursement from a director.⁴⁸ A cease and desist order under 12 U.S.C. § 1818 may be issued under the sole authority of the regulatory agency, and if the party opposes the OCC's order, the party may request an agency hearing.⁴⁹ The text of 12 U.S.C. § 1818 provides that "no court shall have jurisdiction to affect by injunction or otherwise the issuance or enforcement of any notice or order under this section, or to review, modify, suspend, terminate, or set aside any such notice or order."⁵⁰ This section precludes a court from intervening in a regulatory cease and desist order, except as otherwise provided in 12 U.S.C. § 1818. The court in *Larimore* concerned itself with the judicial review that followed the OCC's order. The court was concerned with the procedural safeguards surrounding the reimbursement action if the OCC was acting as the prosecutor, judge, and jury.⁵¹ The court concluded that the OCC could not bring a similar action under another less explicit statute with less procedural safeguards, not only because Congress had already specifically allowed the OCC an avenue to require reimbursement, but because the statute under which the OCC could require reimbursement had the safeguard of requiring the cause to be heard in a federal court.⁵² The court was unwilling to read into 12 U.S.C. § 1818(b)(1) an additional cause of action when Congress had already explicitly provided an avenue for a reimbursement order under 12 U.S.C. § 93(a).

The court in *Larimore* also relied upon the legislative history of 12 U.S.C. § 1818 in denying the OCC the power to require reimbursement under a cease and desist order issued pursuant to this section. The court reasoned that the legislative history of 12 U.S.C. § 1818 does not indicate Congress intended the OCC to assess personal liability against a bank director.⁵³ The court concluded that the statute giving the OCC the power to issue a cease and desist order is only to correct unsafe banking practices, and that the purpose behind 12 U.S.C. § 1818 is to provide the OCC with a method to prevent further deterioration of the financial

case of that kind would either compel the comptroller to forfeit the franchises of the corporation, or suffer its directors to escape liability for a plain violation of law . . . the forfeiture of a bank's franchise, in a suit brought by the comptroller for that purpose, is not, in our judgment, a condition precedent to the maintenance of a suit against its directors for excessive loans.

Cockrill v. Cooper, 86 F. 7, 13 (8th Cir. 1898).

48. 12 U.S.C. § 93(a) (1988).

49. *Id.* § 1818(i)(2)(H) (Supp. II 1990).

50. *Id.* § 1818(i)(1) (Supp. II 1990).

51. *Larimore v. Comptroller of Currency*, 789 F.2d 1244, 1249 (7th Cir. 1986).

52. *Id.* at 1252.

53. *Id.* at 1250

institution.⁵⁴ Courts are reluctant to allow a cause of action to be brought under 12 U.S.C. § 1818 when another statute specifically provides for such cause of action.

In *Citizens State Bank v. Federal Deposit Insurance Corp.*,⁵⁵ the court denied an FDIC order for reimbursement under 12 U.S.C. § 1818(b)(1) for violations of the Truth in Lending Act.⁵⁶ The court reasoned that the existence of another statute specifically addressing violations of the Truth in Lending Act precluded the FDIC's use of 12 U.S.C. § 1818(b)(1).⁵⁷

Prior to the 1989 congressional amendment of 12 U.S.C. § 1818, the usual cases in which courts allowed federal regulatory agencies the authority to require reimbursement under the "take affirmative action" clause, involved bank officials being personally enriched from the illegal activities.⁵⁸ In cases of lending limit violations, it may be difficult to show personal enrichment of the bank official.

In 1989, Congress amended 12 U.S.C. § 1818 to provide a definition of the appropriate actions to be taken under the "take affirmative action" clause and specifically overruled *Larimore*.⁵⁹ Congress amended 12 U.S.C.

54. *Id.* at 1251. The legislative history that the court relied upon provides: "Correctly used . . . these new powers can effectively enhance the ability of the financial institution regulatory agencies to cure unsafe or unsound situations." *Id.* (citing S. REP. NO. 323, 95th Cong., 1st Sess. 7 (1977)).

55. 751 F.2d 209 (8th Cir. 1984).

56. *Id.* at 218.

57. The court stated:

Congress in section 1640 circumscribed the liability of financial institutions by establishing a one-year statute of limitations, 15 U.S.C. § 1640(e) . . . § 1640(b), (c). Reimbursement under section 1818 would be free of all these restrictions so that a financial institution would not be able, as Congress intended, to avoid its liability in the given instance.

Id. When the legislature has specifically provided another avenue for the regulatory agency to pursue, the courts will not allow a broad interpretation of the "take affirmative action" clause to include a reimbursement order.

58. *See, e.g., Hoffman v. Federal Deposit Ins. Corp.*, 912 F.2d 1172, 1174 (9th Cir. 1990) (ordering a bank president to reimburse the bank for funds he received as a result of the bank buying out his employment contract when it appeared eminent that the bank would fail); *First Nat'l Bank of Eden v. Department of Treasury*, 568 F.2d 610, 611 (8th Cir. 1978) (requiring reimbursement for excessive bonuses paid to the bank's president and vice president).

59. The legislative history to 12 U.S.C. § 1818(b)(6) reveals Congress' efforts to clarify the regulatory agencies' authority. The legislative history provides, in pertinent part:

This provision . . . overrules the 7th Circuit Court of Appeals decision in *Larimore v. Comptroller of the Currency*, 789 F.2d 1244 (1986), which held that C&D (cease and desist) authority of the banking agencies did not authorize the OCC to seek in a C&D order reimbursement from a director of a national bank,

§ 1818 to allow a regulatory agency to require a bank official to provide reimbursement if the party was unjustly enriched or if the violation involved a reckless disregard for the law.⁶⁰ The legislative history of this provision reveals an effort to clarify the regulatory agencies' authority.⁶¹ Congress has expressed the necessity for regulatory agencies to seek reimbursement from bank directors who violate banking laws.

IV. OTHER STATES' BANKING STATUTES ANALOGOUS TO INDIANA AND FEDERAL BANKING STATUTES

In 1990, the Illinois Legislature used wording virtually identical to that of the current 12 U.S.C. § 1818 in writing the Illinois Savings Bank Act.⁶² The Illinois statute only applies to savings banks; the Illinois Legislature has not adopted a similar statute for its commercial banks. It is readily apparent from the statute that the Illinois Banking Commissioner may require reimbursement in an order issued to a director of a savings bank when the director violates the bank's legal lending limit and a loss to the bank results. To date, no cases have arisen in which the Illinois Banking Commissioner sought reimbursement from a

who participated in violations of the national Banking Act. The Larimore case has caused confusion in the banking legal community, especially since the underlying conduct in that case did not involve unjust enrichment or harm to the institution. This section would allow such restitution, reimbursement, or indemnification for cases involving unjust enrichment or reckless disregard by the individual involved.

H.R. REP. NO. 54(I), 101st Cong. 1st Sess. at 291, 486 (1989), *reprinted in* 1989 U.S.C.C.A.N. 86, 264.

60. A regulatory agency may require a director to "make restitution or provide reimbursement, indemnification, or guarantee against loss if . . . such depository institution or such party was unjustly enriched in connection with such violation or practice; or, the violation or practice involved a reckless disregard for the law or any applicable regulations." 12 U.S.C. § 1818(b)(6) (Supp. II 1990).

61. *See supra* note 59.

62. ILL. ANN. STAT. ch. 17, para. 7311-1 (Smith-Hurd Supp. 1991). The Illinois statute provides:

The Commissioner is hereby granted authority to issue orders under this Act that requires a savings bank or an institution-affiliated party to take affirmative action to correct any conditions resulting from any violations The order may require . . . the institution-affiliated party to: (1) Make restitution or provide reimbursement, indemnification, or guarantees for or against losses if: (A) the savings bank or the institution affiliated party was unjustly enriched or received direct or indirect personal benefit in connection with the violation or practice; or (B) the violation or practice involved a reckless disregard for applicable laws, regulations, or written agreements or written orders of the Commissioner or other appropriate regulator.

Id.

director for losses resulting from loans made in excess of a bank's legal lending limit.

The Missouri Legislature amended its banking statute in 1990 to define the appropriate actions allowable under the "take affirmative action" clause.⁶³ The amendment is identical to the wording in the Illinois Savings Bank Act and the wording Congress adopted (under FIRREA) in amending 12 U.S.C. § 1818. It is apparent that the Missouri Legislature did not believe that Missouri's State Division of Finance had the appropriate authority to require reimbursement from directors under the previous statute absent the amended language.

The Kentucky Legislature adopted the pre-FIRREA language of 12 U.S.C. § 1818, which allows the Kentucky Department of Financial Institutions to require bank directors to "take affirmative action to correct conditions resulting from such violation or practice."⁶⁴ This Kentucky banking statute does not define the appropriate "affirmative action" that the Kentucky Department of Financial Institutions may require of banking directors. Another Kentucky banking statute allows for director liability for any loss resulting from a violation of a banking statute.⁶⁵ This second statute is somewhat analogous to 12 U.S.C. § 93, but it fails to specifically provide that the Kentucky Department of Financial Institutions can bring suit in its own name to require reimbursement from the directors. The statute only allows Kentucky's Department of Financial Institutions Commissioner to revoke the charter

63. MO. ANN. STAT. § 361.261 (Vernon Supp. 1991)(effective Apr. 30, 1990). The Missouri statute states:

The authority to issue an order under section 361.260 which requires a corporation or any director, officer, employee, agent, or other person participating in the conduct of the affairs of such corporation to take affirmative action to correct any conditions resulting from any violation or practice with respect to which such order is issued includes the authority to require such corporation or such person to: (1) Make restitution or provide reimbursement, indemnification, or guarantee against loss if: (a) Such corporation or such person was unjustly enriched in connection with such violation or practice; or (b) The violation or practice involved a reckless disregard for the law or any applicable regulations or prior order of the director

Id.

64. KY. REV. STAT. ANN. § 287.690(3) (Michie/Bobbs-Merrill 1988).

65. *Id.* § 287.990(5). The statute provides:

Any directors of a bank who knowingly violate, or knowingly permit any officer or employee [sic] of the bank to violate, any of the laws relating to banks, shall be jointly and severally liable to the creditors and stockholders for any loss resulting from such violation. If the loss or damage is not made good within a reasonable time, the commissioner, with the consent of the attorney general, shall institute proceedings to revoke the corporate powers of the bank.

Id.

of a bank whose directors refuse to comply with a reimbursement order.⁶⁶ To date, no cases have been reported in which the Kentucky Department of Financial Institutions sought reimbursement from directors for losses resulting from lending limit violations.

Ohio's banking laws have a provision analogous to Kentucky's in that a cease and desist order may require the bank directors to "take affirmative action to correct the conditions resulting from any such violation."⁶⁷ Ohio also has a statute providing for the personal liability of directors.⁶⁸ However, this statute does not explicitly indicate that the Ohio Banking Department may bring suit in its own name against directors who violate a banking statute which results in a loss to the bank before the bank is placed in receivership. Ohio's statutes create the same dilemma as Kentucky's in that the court will have to take an expansive view of the "take affirmative action" language, in light of the existence of another statute, in order to provide the Ohio Banking Department with an avenue for bringing a reimbursement action against a bank director.

Michigan law, as well as Ohio and Kentucky law, contains the "take affirmative action" clause with no definition of the extent of affirmative action that the Michigan Financial Institutions Bureau may request.⁶⁹

66. Indiana's statutes differ in that they grant the DFI authority to take possession of a bank that violates banking laws but the statutes do not specifically authorize such action for the failure of bank directors to make reimbursements to the bank as does the Kentucky banking statute. *See supra* note 30.

67. OHIO REV. CODE ANN. § 1125.08 (Anderson 1988). The Ohio law states: [T]he superintendent may issue and serve upon the bank or regulated individual an order to cease and desist from any such violation or practice. Such order may, by provisions which may be mandatory or otherwise, require the bank and its directors, officers, employees, and agents, or the regulated individual, to cease and desist from the same, and, further, to take affirmative action to correct the conditions resulting from any such violation or practice.

Id.

68. *Id.* § 1115.06. This statute provides: Any member of the board of directors of a bank who knowingly violates or knowingly permits any of the officers, agents, or employees of the bank to violate any of the provisions of Chapters . . . shall be liable in his personal and individual capacity for all damages which the bank, its shareholders, or any other person sustains in consequence of such violation.

Id.

69. MICH. COMP. LAWS ANN. § 487.335 (West 1987). The Michigan statute provides: [T]he commissioner may issue and serve upon the institution an order to cease and desist from any such practice or violation. By provisions which may be mandatory or otherwise, the order may require the institution and its directors, officers, employees and agents to cease and desist from the same and to take affirmative action to correct the conditions resulting from any such practice or violation.

Id.

Michigan also has a statute allowing for the personal liability of directors and provides that such suit may be brought by "any shareholder or any other person [who] sustains [damages] in consequence of the violation."⁷⁰ The Michigan Financial Institutions Bureau will have to claim that it suffered some damage in order to have standing to bring suit under this statute.

Illinois and Missouri have taken the lead in adopting the language of the federal statute defining the appropriate remedies allowed under the "take affirmative action" clause. Indiana, as well as Ohio, Kentucky, and Michigan, has not adopted a definition of what "affirmative action" is appropriate for banking regulators to require of bank directors. The intention of the Indiana General Assembly is unclear because it failed to follow Congress, as the Illinois Legislature did, in adopting the federal amendments to 12 U.S.C. § 1818. Various explanations for this lack of clarification may exist. An explanation may be that the Indiana lawmakers wished to confer on the Indiana Department of Financial Institutions (DFI) broad powers in carrying out its functions. This interpretation, giving bank regulators broad powers, has support at the federal level as seen in *del Junco v. Conover* and in Congress' actions of amending 12 U.S.C. § 1818 to specifically overrule the holding in *Larimore v. Comptroller of Currency*.⁷¹

V. PROPOSAL FOR THE INTERPRETATION OF INDIANA'S BANKING STATUTES THAT WILL PROVIDE THE DFI WITH A CAUSE OF ACTION

The failure of the Indiana General Assembly to adopt a definition for appropriate action that the DFI may request under the "take affirmative action" clause is confusing at best. Either the legislature thought that the DFI already had this authority or the legislature did not wish the DFI to be able to order reimbursement from directors. The legislature could have easily provided explicit language to indicate either of these options, yet the legislature chose to leave the "take affirmative action" clause undefined. Although "affirmative action" may include establishing

70. *Id.* § 487.513. Personal liability is imposed by the following language: If the directors or officers of a bank knowingly violate, or knowingly permit any of the agents, officers or directors of a bank to violate, any of the provisions of this act or rules of the commissioner made under authority thereof, every director and officer who participated in or assented to the violation shall be held liable in his personal and individual capacity for all damages which the bank, any shareholder or any other person sustains in consequence of the violation. Any action to recover damages shall be brought within 3 years from the time of the violation, and not afterwards.

Id.

71. See *supra* notes 37-54 and accompanying text.

loan policies or increasing the level of capital, the language may also contemplate requiring directors to reimburse the bank for losses sustained as a result of lending limit violations.

Congress contemplated federal regulatory agencies seeking reimbursement orders and explicitly provided such authority in 12 U.S.C. § 93, and also in 12 U.S.C. § 1818. It is difficult to believe that the Indiana Legislature chose to preclude the DFI from having the authority to take similar action.

In 1991, when the legislature gave the DFI the power to assess civil monetary penalties, the legislature also gave the DFI the power to issue an order requiring a bank director to "take affirmative action to correct the conditions resulting from the practice or violation."⁷² Because the legislature provided for the assessment of CMPs in the same statute that allows an order to require the directors to "take affirmative action," the legislature must have intended the "take affirmative action" clause to allow for reimbursement orders.

A comparison of the high limit of penalties that federal regulatory agencies may impose with the relatively low limit that the DFI may impose further indicates that the legislature did not wish to preclude reimbursement actions under the "take affirmative action" clause.⁷³

72. IND. CODE § 28-11-4-7(c)(1)(B) (West Supp. 1992). *See supra* note 24.

73. The federal statute allowing civil monetary penalties was amended by FIRREA and now reads as follows:

(A) First tier. Any insured depository institution which, and any institution-affiliated party who-

- (i) violates any law or regulation;
- (ii) violates any final order or temporary order issued pursuant to subsection (b), (c), (e), (g), or (s) of this section;
- (iii) violates any condition imposed in writing by the appropriate Federal banking agency in connection with the grant of any application or other request by such depository institution; or
- (iv) violates any written agreement between such depository institution any such agency,

shall forfeit and pay a civil penalty of not more than \$5,000.00 for each day during which such violation continues.

(B) Second tier. Notwithstanding subparagraph (A), any insured depository institution which, and any institution-affiliated party who—

- (i)(I) commits any violation described in any clause of subparagraph (A); (II) recklessly engages in an unsafe or unsound practice in conducting the affairs of such insured depository institution; or (III) breaches any fiduciary duty;
- (ii) which violation, practice, or breach—(I) is part of a pattern of misconduct; (II) causes or is likely to cause more than a minimal loss to such depository institution; or (III) results in pecuniary gain or other benefit to such party,

shall forfeit and pay a civil penalty of not more than \$25,000 for each day during which such violation, practice, or breach continues.

(C) Third tier. Notwithstanding subparagraphs (A) and (B), any insured depository

Federal regulators may impose penalties up to \$1,000,000. If the purpose of the Indiana statute is to deter violations, the legislature should have followed Congress' lead and adopted a higher penalty limit. Regulators may assess penalties regardless of whether the violation has resulted in the bank losing money. The DFI should be given the option of either imposing penalties or seeking reimbursement, whichever remedy the DFI determines to be most effective to address the specific situation.

Because the DFI is given such an onerous task as ensuring the solvency of the state's financial institutions, a broad interpretation of the DFI's authority is warranted. The legislature may have specifically left the "take affirmative action" clause broad and ambiguous to allow the DFI to fashion an appropriate remedy in situations such as lending limit violations.⁷⁴

The function of the DFI is to ensure the financial soundness of the bank. Therefore, waiting for the bank to fail in order for the DFI to bring suit against the directors is inconsistent with the DFI's function. The DFI should be able to take immediate action to mitigate the possibility of a bank failure. A bank may still be harmed even if the directors' actions do not result in jeopardizing the bank's viability. Consequently, the DFI, the only entity aside from the bank directors with possible knowledge of the violation, should be allowed to pursue a reimbursement order. Although the DFI may not suffer direct loss, the directors' violations of the applicable banking statutes impinge upon

institution which, and any institution-affiliated party who—

(i) knowingly—(I) commits any violation described in any clause of subparagraph (A); (II) engages in any unsafe or unsound practice in conducting the affairs of such depository institution; or (III) breaches any fiduciary duty; and

(ii) knowingly or recklessly causes a substantial loss to such depository institution or a substantial pecuniary gain or other benefit to such party by reason of such violation, practice, or breach, shall forfeit and pay a civil penalty in an amount not to exceed to applicable maximum amount determined under subparagraph (D) for each day during which such violation, practice, or breach continues.

(D) Maximum amounts of penalties for any violation described in subparagraph (c). The maximum daily amount of any civil penalty which may be assessed pursuant to subparagraph (C) for any violation, practice, or breach described in such subparagraph is— (in the case of any person other than an insured depository institution, an amount to not exceed \$1,000,000. . . .

12 U.S.C. § 1818(i)(2) (Supp. II 1990).

74. *Cf.* *Foremost Life Ins. v. Department of Ins.*, 409 N.E.2d 1092, 1096 (Ind. 1980) ("[A] statute is to be examined and interpreted as a whole, giving common and ordinary meaning to words used . . ."); *Thompson v. Thompson*, 286 N.E.2d 657, 661 (Ind. 1972) ("The foremost object of construing a statute is to determine and carry out the true intent of the Legislature.").

the DFI's duties of protecting the financial institution and ensuring the public's confidence in the financial system.

The DFI and the Office of the Comptroller of the Currency (OCC), through regulation, attempt to ensure the soundness of the state and national banking systems respectively. Since 1864, the OCC has had the authority to seek reimbursement from directors.⁷⁵ The similarity of duties the OCC and the DFI perform in regulating banks reveals that the DFI should be allowed to seek reimbursement from directors when the bank sustains a loss on a loan made in excess of the bank's legal lending limit. The DFI must take action before losses to the bank become even greater.

The Seventh Circuit decided *Larimore v. Comptroller of Currency* in 1986, and Congress adopted FIRREA in 1989. Yet, when the Indiana General Assembly amended the Indiana banking statute in 1991, it did not provide explicit language to define the proper remedies under the "take affirmative action" clause. Portions of the Indiana banking statutes utilize virtually identical language as portions of the federal banking statutes that provide for the requirement of taking "affirmative action." Because of the conflicting interpretations in *del Junco* and *Larimore* of the "take affirmative action" clause,⁷⁶ the Indiana lawmakers should have provided some guidance on the appropriate remedies for the DFI to utilize. Indiana courts may find room to broaden the interpretation of the "take affirmative action" clause in the absence of any other statute allowing the DFI to seek reimbursement.

The division of the federal circuits in interpreting the "take affirmative action" clause and the Ninth Circuit's reaffirmation of its decision in *del Junco* after Congress amended the federal banking statutes in 1989 to overrule *Larimore*, supports the interpretation that the "take affirmative action" clause contemplates regulatory agencies seeking reimbursement in their administrative orders.

The Indiana statutes provide judicial review that 12 U.S.C. § 1818 precludes, and about which the court in *Larimore* was concerned.⁷⁷ The procedural safeguard question does not arise because no other statute in Indiana allows the DFI to utilize greater procedural safeguards. The current Indiana statute, although analogous to the pre-FIRREA 12 U.S.C. § 1818, should allow the DFI to bring suit in its own name requesting reimbursement from directors who have violated the bank's legal lending limit.⁷⁸

75. 12 U.S.C. § 93(a) (1988).

76. See *supra* notes 37-54 and accompanying text.

77. IND. CODE § 28-11-4-8(c) (Supp. 1992).

78. If the legislature decides that the DFI should not be given the authority to

Banking is a regulated industry and allowing a regulatory agency, such as the DFI, the authority to sue bank directors in their individual capacity does not unduly increase the burden of regulation. National bank directors are already subject to such liability. The proposed cause of action for the DFI provides a remedy for any harm caused as a result of loans made in excess of the bank's legal lending limit. Personal liability only becomes an issue after a bank director violates a lending limit statute. Because bank directors may currently violate state banking laws and avoid the consequences of their actions, the DFI should be given the authority to sue directors in their personal capacity.

Bank directors have the duty to comply with applicable banking laws and should not escape liability if they breach this duty. The directors should be charged with correcting the condition resulting from the violation. The notion of director reimbursement is not a foreign concept because shareholders who have knowledge of such violation can sue directors to recover for any losses resulting from lending limit violations.⁷⁹

bring suit in its own name against directors who have violated the bank's legal lending limit, the legislature should at least consider amending the restrictions on the disclosure of examination material. Congress has realized that disclosure of administrative actions actually benefits compliance. Shareholders, creditors, and depositors will have adequate information to decide whether to seek a reimbursement suit against directors if regulators increase the public disclosure of examination information.

In § 913 of the FIRREA, Congress increased the public disclosure of final enforcement orders and provided the following explanation:

The bank regulatory agencies, with infrequent exceptions, do not disclose civil enforcement actions. (They are the only Federal regulatory agencies which do not do so.) [sic] This policy and [sic] has been specifically criticized in congressional reports and during congressional hearings. One of the problems in the financial services industry (except for SEC-regulated institutions, which must disclose such enforcement actions) has been the excessive secrecy of agency supervisory actions. Such secrecy does little to deter misconduct, but does serve to ultimately worsen the problems of financial institutions. The October 1988 Government Operations Committee report specifically recommended legislation to require the banking agencies to publicly disclose all formal civil enforcement actions and any modifications to or terminations of such orders. Disclosure could be delayed only in those rare instances where it would imminently jeopardize the institution's solvency. The Committee strongly believes that more disclosure of formal enforcement orders will help prevent insider misconduct.

H.R. REP. No. 54(I), 101st Cong. 1st Sess. 291, 470 (1989), *reprinted in* 1989 U.S.C.C.A.N. 86, 266. Annual reports may provide shareholders with some access to information regarding loan losses. However, losses resulting from loans made in excess of the lending limit most likely will not be separated in such a report to provide the shareholder with adequate information to bring suit. Absent any "red flag" to the shareholder, it may be difficult, if not impossible, to force disclosure of any losses occurring from loans made in excess of the bank's legal lending limit. Therefore, allowing the DFI to bring suit would be the most effective means of enforcement.

79. Because the DFI's function is to ensure the soundness of financial institutions,

VI. CONCLUSION

There is a void of case law concerning state banking departments bringing suit against directors personally for violations of banking statutes that result in losses to the bank but do not cause the insolvency of the bank. The parties who have greatest access to the violations and resulting losses, the regulators, are often unable by statute to disclose this information to stockholders and others who may then bring an action against the bank directors. Because banking departments are charged with ensuring the safety and soundness of financial institutions, they should have the authority to bring suit against directors requiring reimbursement before the condition of the bank deteriorates to a point of being placed in receivership.

In Indiana, the assessment of civil monetary penalties is too narrowly directed toward deterrence and does nothing about correcting the condition resulting from the violation of a banking statute.

The current language of Indiana's banking statutes may present difficulties if the DFI wishes to bring suit against bank directors and require reimbursement for losses resulting from violations of the bank's lending limit. However, the federal cases that have interpreted similar language have relied upon the existence of another statute that allowed the regulator another avenue to bring a reimbursement action. Absent a similar statute in Indiana, the courts may find that the legislature intended the DFI to bring reimbursement actions under the "take af-

the DFI is essentially performing a function of the FDIC by protecting the FDIC insurance fund. The FDIC fund protects depositors; therefore, the DFI is indirectly protecting depositors. The DFI should be given whatever authority is necessary to ensure the soundness of each state banking institution because of the great interest in protecting depositors. Although protecting depositors, the DFI is indirectly protecting shareholders. Private investors in public corporations do not receive government protection. However, to ensure the stability of the banking system, it is necessary for the DFI to provide some protection for depositors. This protection is warranted even if it also benefits shareholders. Allowing reimbursement from directors provides the DFI with a means to alleviate the adverse effects of lending limit violations.

The matter of how far the state banking departments should go in protecting depositors who are already insured by the FDIC fund may be analogous to the question of how far the FDIC should go in protecting depositors who are uninsured (i.e., have in excess of \$100,000 on deposit at a single financial institution).

In a statement by Robert Clarke, Comptroller of the Currency, before the Subcommittee on Economic Stabilization, House Committee on Banking, Finance and Urban Affairs, concerning deposit insurance of uninsured depositors, he stated: "Too little protection could threaten the stability of financial markets; too much protection raises serious questions about competitive equity, can reduce incentives for uninsured depositors to monitor the riskiness of institutions, and has the potential to strain the resources of the federal deposit insurer." *Speeches and Congressional Testimony*, 10 Q. J. No. 3 at 35 (1991).

firmative action" statute. In any event, the Indiana General Assembly should take the lead of Congress, the Illinois Legislature, and the Missouri Legislature and amend the Indiana banking statutes to explicitly allow the DFI to bring a reimbursement action against directors before the bank is insolvent or placed in receivership.