

OFFICE OF THRIFT SUPERVISION

Approval of Holding Company Application, Bank Merger Act Application, And Related Filings

Order No.: 2002-66
Date: December 20, 2002
Docket Nos.: H-3730, H-3731, 01272,
H-2835, H-2230

Northwest Bancorp, MHC, Warren, Pennsylvania (Holding Company) has applied pursuant to 12 U.S.C. § 1467a(e) and 12 C.F.R. § 574.3, for approval of the Office of Thrift Supervision (OTS) to acquire Leeds Federal Savings Bank, Baltimore, Maryland (Association). In addition, the Association has applied pursuant to 12 U.S.C. § 1828(c) and 12 C.F.R. § 563.22(a), for OTS approval of the merger of an interim federal savings association (Interim) with and into the Association. The Association has also applied to OTS to make a capital distribution under the OTS Capital Distribution Regulations. (The foregoing filings are collectively referred to as the Applications.)

The Applications

The Holding Company, the top-tier holding company in a federally chartered mutual holding company structure, owns approximately 74.6 percent of Northwest Bancorp, Inc., Warren, Pennsylvania (Mid-Tier 1), a mid-tier, federally chartered mutual holding company, which owns all of the common stock of Northwest Savings Bank, Warren, Pennsylvania (Savings Bank) and all of the common stock of Jamestown Savings Bank, Jamestown, New York (Jamestown). The Savings Bank and Jamestown elected to be treated as savings associations under section 10(l) of the Home Owners' Loan Act (HOLA), in June 2001. (OTS Order No. 2001-40, May 24, 2001.)

The Holding Company proposes to acquire by merger Leeds Federal Bancshares, MHC, Baltimore, Maryland (MHC). MHC is the parent of Leeds Federal Bancshares, Inc., Baltimore, Maryland (Mid-Tier 2), a mid-tier federally chartered mutual holding company. MHC owns 72.7 percent of Mid-Tier 2, with the remaining shares held by minority shareholders (Minority Shareholders). In order to consummate the transaction, Mid-Tier 2 will conduct a reverse stock split in which each share of Mid-Tier 2 common stock held by Minority Shareholders will be converted into the right to receive \$32.00 in cash. Mid-Tier 2 will fund the payment with a dividend from the Association. Mid-Tier 2 will then convert into the Interim, which will merge with and into the Association, with the Association being the resulting entity. Immediately thereafter, MHC will merge with and into the Holding Company, with the Holding Company being the resulting entity, and the Association will become a direct subsidiary of the Holding Company. As a result of the transaction, the interests of the Association's

depositors as members of MHC will cease to exist and will be converted into interests of the Holding Company.

Two commenters, Fulton Savings Bank, Fulton, New York, and Hartford Financial Management, Inc. submitted comments asserting that OTS should not approve the Applications, stating that mutual holding company members are not adequately protected or represented in this type of transaction, and that insiders are allowed to profit unfairly in such transactions. The comments raise issues that OTS has already considered. In response to a previous inquiry urging OTS to impose a moratorium on transactions of this nature, OTS stated that it does not plan to impose a moratorium.

Holding Company Application

The Holding Company's acquisition of the Association requires OTS approval under section 10(e) of the HOLA, and the OTS regulations thereunder (Control Regulations).

Section 10(e) of the HOLA and the Control Regulations require that OTS consider, with respect to the Holding Company's acquisition of the Association, the financial and managerial resources and future prospects of the Holding Company, the Savings Bank, Jamestown and the Association, the effect of the acquisition on the savings associations, the insurance risk to the Savings Association Insurance Fund (SAIF) and Bank Insurance Fund (BIF), and the convenience and needs of the community to be served. OTS also must consider the impact of the acquisition on competition. Further, 12 C.F.R. § 563e.29(a) requires that the OTS take into account assessments under the Community Reinvestment Act (CRA) when approving holding company acquisitions.

As for managerial resources, OTS, in its role as the regulator of the Holding Company and the Association, is familiar with their managerial resources. Upon consummation of the acquisition of the Association, the board of directors and the executive officers of the Holding Company, Jamestown, and the Savings Bank will consist of the present directors and executive officers of the Holding Company, Jamestown, and the Savings Bank. Three of the Association's current directors will retire. Two senior officers of the Savings Bank and one senior officer of the Association will become directors of the Association. OTS also has considered the managerial resources of the Savings Bank and Jamestown, which will not change as a result of the proposed transaction. Based on the foregoing, OTS concludes that the managerial resources of the Holding Company and the three savings associations are consistent with approval.

As for financial resources, OTS is familiar with the financial resources of the Holding Company and the Association. As of June 30, 2002, the Holding Company's shareholders equity equaled 7.3 percent of its assets and its tangible capital ratio was 5.8 percent. The Savings Bank and Jamestown are both well-capitalized. Upon consummation of the transaction, the Association will have core capital of 5.18 percent

and risk-based capital of 9.63 percent. The Holding Company intends to make a capital contribution of \$15.0 million to the Association at the conclusion of the transaction. OTS is imposing condition 8, below, requiring the Association to be well capitalized under the OTS Prompt Corrective Action regulations immediately upon consummation of the transaction, and for the following three years. Based on the foregoing, OTS concludes that the financial resources of the Holding Company and the three savings associations are consistent with approval, subject to imposition of the conditions set forth below.

Based on its consideration of the managerial and financial resources of the Holding Company and the three savings associations, OTS concludes that the future prospects of the Holding Company and the associations, and the effect of the transaction on the SAIF and BIF are consistent with approval, provided that OTS imposes the conditions set forth below.

As for the competitive impact of the transaction, there is no overlap in market areas of the Savings Bank and Jamestown, and the Association. The Department of Justice's competitive factors report has not objected to the transaction. Accordingly, OTS concludes that the transaction is not objectionable on competitive grounds.

As for CRA considerations in connection with the holding company application, the Savings Bank's and Jamestown's most recent CRA ratings are "Satisfactory." No comments objecting to the Applications on the basis of CRA have been filed. Accordingly, OTS concludes that approval of the holding company application is consistent with the CRA.

As for convenience and needs, the operations of the Association's existing offices and the existing services to the Association's customers and communities will continue. Accordingly, OTS concludes that approval of the transaction is not objectionable based on convenience and needs considerations.

Formation of Interim Association, and Merger Application

The formation of the Interim requires OTS approval under 12 C.F.R. § 552.2-2. The merger of the Interim into the Association requires OTS approval under section 18(c) of the Federal Deposit Insurance Act (FDIA) (Bank Merger Act or BMA), and 12 C.F.R. § 563.22(a).

With respect to formation of the Interim, 12 C.F.R. § 552.2-2 provides that approval of an application to organize an interim federal stock savings association shall be conditioned upon approval by OTS of an application to merge the interim, or upon approval of another transaction that the interim was designed to facilitate. OTS has previously approved several similar transactions involving the conversion of federal mutual holding companies into interim associations, and concludes that the proposed transaction is consistent with 12 C.F.R. § 552.2-2.

With respect to the merger of the Interim into the Association, the Bank Merger Act and the OTS regulations thereunder impose standards of approval that are substantially similar to the holding company approval standards.¹ The USA Patriot Act (Act) amended the Bank Merger Act, adding 12 U.S.C. § 1828(c)(11), which requires the responsible agency to take into consideration, in its evaluation of the BMA application, the effectiveness of any insured depository institution in combating money laundering activities. In addition, under OTS regulations, OTS must consider whether the merger is equitable to all concerned, whether full disclosure has been provided regarding written or oral agreements through which any person will receive anything of value in connection with the transaction, whether compensation to officers, directors, and controlling persons of the disappearing association is reasonable, and whether provisions regarding advisory boards are consistent with the regulations.² The CRA requires, in the context of the merger transaction, that OTS consider the CRA performance of the Association.³

Because the Interim would be a shell entity, the merger of the Interim into the Association will have no material effect on the managerial and financial resources and future prospects of the Association and the Interim, nor will the merger have any effect on competition or on the convenience and needs of the community.

As for equitable treatment, the transaction is a component of another transaction that was negotiated at arms-length. With respect to full disclosure regarding written or oral agreements or understandings through which any person or company will receive anything of value in connection with the proposed transaction, materials distributed in the context of the minority shareholder and depositor votes provided relevant information. As for employment contracts and advisory boards, the merger of the Interim and the Association will not result in any employment contracts or advisory boards.

With respect to compliance with money laundering statutes and regulations, OTS examines savings associations for compliance with such statutes and regulations. OTS' review of the Association's compliance with money laundering statutes and regulations has not revealed any matters that are inconsistent with approval of the merger application.

With respect to the CRA, the Association received a "Needs to Improve" rating at its latest CRA examination. After that examination, however, OTS has reviewed the Association's response to its CRA evaluation, and has found that the Association has taken positive steps toward improving its CRA performance. Moreover, the Applications indicate that the Holding Company will take the necessary steps to ensure that the Association will improve its CRA rating. No commenters have objected to the merger on CRA grounds. Accordingly, OTS concludes that approval of the merger application is consistent with the CRA.

¹ 12 U.S.C. § 1828(c)(5)(B); 12 C.F.R. § 563.22(d) (2002).

² 12 C.F.R. § 563.22(d)(1)(vi) (2002).

³ See 12 C.F.R. § 563e.29(a)(2002).

Capital Distribution Notice

The Association seeks OTS approval to make a capital distribution of \$46.5 million to pay the Minority Shareholders for their common stock and to pay certain transaction expenses. The OTS Capital Distribution Regulations require OTS to consider a savings association's capital position upon completion of the capital distribution, the effects of the capital distribution on the safety and soundness of the savings association, and the conformity of the capital distribution with applicable statutes, regulations, and other limitations. Based on the Association's capital position after the transaction, relevant safety and soundness considerations, and the fact that the distribution does not violate any relevant statute, regulations, or other provision, OTS concludes that the Association's proposed capital distribution in connection with the proposed transaction is consistent with approval, provided that the Association complies with condition 8, below.

Mutual Holding Company Considerations

Section 575.10 of OTS' regulations provides authority for the transaction.⁴ The regulation explicitly authorizes a federal mutual holding company to acquire another mutual holding company by merger.

OTS regulations, at 12 C.F.R. §§ 575.5(a)(2) and (a)(4), require, under these circumstances, that depositors and borrowers of the Association who currently have membership rights in MHC, receive, after the transaction, the same membership rights in the Holding Company they had immediately prior to the transaction.

In this case, the members of MHC currently have voting rights, but members of the Holding Company do not. Although the Holding Company will draw members from the Association after the transaction, depositors and borrowers of the Association will no longer have voting rights, except in the event of a second step stock conversion of the Holding Company, placing them in the same position as depositors and borrowers of the Savings Bank and Jamestown. The proposed arrangement regarding the rights of depositor and borrower members of MHC, therefore, is not consistent with 12 C.F.R. §§ 575.5(a)(2) and (a)(4).

OTS regulations, at 12 C.F.R. § 575.1(b), provide that OTS may waive (non-statutory) requirements of the Mutual Holding Company Regulations for good cause. The § 575.5(a)(2) and § 575.5(a)(4) requirements are not statutory. In the absence of a waiver, MHC's depositor and borrower members (Members), alone among those of the three depository institution subsidiaries of the Holding Company, would have voting rights. The Holding Company proposes to treat Members the same as depositors and member borrowers of the Holding Company's other depository institution subsidiaries. Members will have the opportunity to vote on the proposed transaction, and have been provided with a proxy that explicitly describes the loss of voting rights. Based on the foregoing, OTS has concluded that good cause to grant the waivers exists.

⁴ 12 C.F.R. § 575.10(a)(3) (2002).

Conclusions

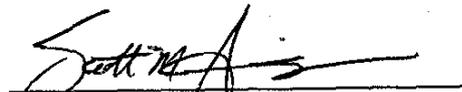
Based on the foregoing analysis, OTS concludes that each of the foregoing Applications meet the applicable approval criteria. However, consummation of the transaction in the manner proposed would be inconsistent with 12 C.F.R. §§ 575.5(a)(2) and 575.5(a)(4), and for the reasons discussed above, OTS, pursuant to 12 C.F.R. § 575.1(b), hereby waives these two regulatory provisions to permit the depositor and borrower members of MHC to have the same rights as members of the Holding Company whose rights with the Holding Company are derived from the Savings Bank or Jamestown. Accordingly, the Applications, are hereby approved, provided that the following conditions are complied with in a manner satisfactory to the Southeast Regional Director, or his designee (Regional Director):

1. The Holding Company, the Savings Bank, MHC, Mid-Tier-1, Mid-Tier-2, and the Association must receive all required regulatory and shareholder approvals for the proposed transaction and submit copies of such approvals to the Regional Director prior to the consummation of the proposed transaction;
2. The proposed transaction must be consummated no later than 120 days from the date of this Order;
3. Prior to consummation of the proposed transaction, a final executed tax opinion addressing the tax consequences of the transaction to the Association must be submitted to the Regional Director;
4. On the business day prior to the date of consummation of the proposed transactions, the chief financial officers of the Holding Company, the Savings Bank, MHC, Mid-Tier-1, Mid-Tier-2, and the Association must certify in writing to the Regional Director that no material adverse events or material adverse changes have occurred with respect to the financial condition or operations of their respective entities, since the date of the financial statements submitted with the applications. If additional information having a material adverse bearing on any feature of the applications is brought to the attention of the Holding Company, the Savings Bank, MHC, Mid-Tier-1, Mid-Tier-2, the Association or OTS since the date of the financial statements submitted with the Applications, the transaction must not be consummated unless the information is presented to the Regional Director, and the Regional Director provides written non-objection to consummation of the transaction;
5. The Holding Company and the Savings Bank must advise the Regional Director in writing within five calendar days after the effective date of the proposed transaction (a) of the effective date of the transaction and (b) that the transaction was consummated in accordance with all applicable laws, regulations, the Applications and this Order;

6. Within 60 calendar days from the date of consummation of the transaction, the Holding Company must submit a report from its independent auditor, satisfactory to the Regional Director, that indicates that the Holding Company accounted for the transaction in accordance with generally accepted accounting principles. This report should include reasonable detail to describe the accounting impact of the transaction as of the effective date of the transaction, including the amount of goodwill and other intangible assets created by the transaction;
7. Should the Holding Company and the Association establish a tax sharing arrangement with a written tax sharing agreement, such an agreement will first be submitted to the Regional Director for non-objection;
8. Immediately upon consummation of the proposed transactions, and for the three years thereafter, the Association must maintain well capitalized status, as that term is defined in 12 C.F.R. Section 565.4;
9. Upon completion of the organization of the Interim federal savings association, the boards of directors of the Association and the Interim federal savings association must ratify the agreement and plan of merger; and
10. Not later than 5 calendar days after the date of consummation of the merger of the Interim and the Association, the Association must submit a certification of legal counsel stating: (a) the effective date of the merger; (b) that the Interim federal savings association never opened for business; and (c) that the merger has been consummated in accordance with the Application, applicable state law, applicable federal law, and this Order.

Any time period set forth herein may be extended for up to 120 calendar days, for good cause, by the Regional Director.

By order of the Director of the Office of Thrift Supervision, or his designee,
effective December 20, 2002



Scott M. Albinson
Managing Director
Office of Supervision