

COMMONWEALTH OF KENTUCKY
PUBLIC PROTECTION CABINET
DEPARTMENT OF FINANCIAL INSTITUTIONS
AGENCY CASE NO. 2016-AH-00081



DEPARTMENT OF FINANCIAL INSTITUTIONS

COMPLAINANT

V.

LOUISA COMMUNITY BANK, INC.,
GENE A. WILSON, Individually, and
KATHRYN REID, Individually

RESPONDENTS

**DEPUTY COMMISSIONER'S FINDINGS OF FACT,
CONCLUSIONS OF LAW, AND FINAL ORDER**

An Administrative Hearing was held in this matter on May 11, 2017, at the Department of Insurance, 215 West Main Street, Frankfort, Kentucky. The Complainant, Department of Financial Institutions ("DFI" or "Department"), was represented by Gary A. Stephens, Staff Attorney, and former DFI General Counsel Tiffany Ge. Charles Vice, Commissioner of DFI, was the Department's representative. The Respondents, Gene A. Wilson and Kathryn Reid, were represented by Stephen B. Pence, Attorney at Law. Tim Cocanougher, Hearing Officer, Public Protection Cabinet, presided.¹

The subject of the hearing was DFI's Notice of Assessment of Fines charging that Wilson and Reid had violated Joint Consent Orders entered into by Respondents, DFI, and the Federal Deposit Insurance Corporation ("FDIC"). On October 19, 2017, the Hearing Officer, having reviewed the record, including all exhibits and written submissions by the parties, issued a Recommended Findings of Fact, Conclusions of Law, and Recommended Order ("Recommended Order"). After careful consideration of the record, including the Recommended Order and the

¹ DFI settled its claims against Louisa Community Bank, another original Respondent in the action, prior to the May 11, 2017 hearing. As used herein, "Respondents" will refer only to Wilson and Reid.

duly filed exceptions, for the reasons set forth herein, the Department's Deputy Commissioner hereby enters this Findings of Fact, Conclusions of Law, and Final Order adopting, in part, and modifying, in part, the Hearing Officer's Recommended Order.²

FINDINGS OF FACT

A. Background and Joint Consent Orders.

As accurately observed in the Recommended Order, Respondent Gene Wilson was a founding shareholder and chairman of the first board of directors of Louisa Community Bank ("Bank of Louisa" or "Bank"). At all relevant times herein, Wilson and Respondent Kathryn Reid served on the bank's board of directors, and were also majority shareholders. (Recommended Order at 2).

In 2014, the Bank began having difficulties and was designated by DFI and FDIC as a "troubled bank," leading to the first Joint Consent Order into which the parties entered on December 11, 2014. (DFI's Hearing Exhibit 1). DFI Commissioner Vice testified that a consent order, which is essentially an agreement between a bank and its regulators, serves as a regulatory tool utilized by the FDIC and DFI to address concerns raised in bank examinations. (Hearing Transcript, p. 15-16). Respondents Wilson and Reid were members of the Bank's board of directors who, with the rest of the board, signed the 2014 Consent Order on behalf of the Bank. (Hearing Transcript, p. 18). This Order placed a number of restrictions on the Bank and, with regard to its management, states:

Prior to the addition of any individual to the board of directors or the employment of any individual as a senior executive officer, the Bank shall request and obtain the written approval of the Regional Director of the FDIC Chicago Regional Office

² As set forth in a May 10, 2017 letter to the Hearing Officer, because agency head, DFI Commissioner Vice, testified as a witness in the administrative hearing of this matter, he has delegated for purposes of this administrative action, pursuant to KRS 286.1-025, all the duties and powers of the Commissioner (agency head), including those listed in KRS 13B.030, to DFI Deputy Commissioner, Brian Raley. This Final Order is therefore being entered by Deputy Commissioner Raley.

(“Regional Director”) and the KDFI...”

(DFI’s Hearing Exhibit 1 at 3) (emphasis added). Commissioner Vice testified that these provisions are included in a consent order with a bank dealing with management issues to: (1) “slow the bank down;” (2) promote stability with the management team and the board of directors; and (3) communicate to the bank that the regulators and the bank need to work together to solve the management issues. (Hearing Transcript, p. 20) (Recommended Order at 2-3).

The Bank entered into a second Joint Consent Order with DFI and FDIC on January 29, 2016 (DFI’s Hearing Exhibit 2), which was also signed by the Bank’s board of directors, including Wilson and Reid. (Recommended Order at 2). Commissioner Vice explained that this 2016 Order was the result of “an unusual situation,” which arose from an examination of the Bank conducted after the initial 2014 Order had been put in place. DFI and FDIC agreed that, in light of the subsequent examination, they “needed to provide additional direction to the bank on how to address their problems.” (Hearing Transcript, p. 22). Among other things, the 2016 Consent Order included a provision that required the Bank to:

maintain a board of directors which is composed of at least five (5) directors, as required by KRS 286.3, and . . . contain at least two fifths (2/5) members who are independent directors....

(DFI’s Hearing Exhibit 2 at 3) (Recommended Order at 2). Commissioner Vice testified that this provision is not a typical component of a consent order, but rather was included in the 2016 Order based upon statements Respondent Wilson had made at a preceding Bank of Louisa Board meeting. (Recommended Order at 3). Specifically, Wilson had announced at an earlier Board meeting that he needed to restructure the board and planned to: (a) reduce the number of board members to five; and (b) add a number of individuals he personally wanted on the board. (Hearing

Transcript, p. 23). The 2016 Consent Order also contained a provision regarding the procedures to be followed should the Bank lose a director:

If necessary, the Bank shall, within sixty (60) days of losing any director, request and obtain the written approval of the Regional Director and the KDFI to add a new individual to the Board, as required by Paragraph 1(b) of the ORDER. If written approval is granted by the Regulators, the Bank shall then comply with all requirements of Section 32 of the FDI Act.

(DFI's Hearing Exhibit 2 at 3). Notably, the 2016 Order did not replace the existing 2014 Consent Order, but rather supplemented it, simultaneously placing the Bank under the provisions of both. As correctly noted by the Hearing Officer, both of the Consent Orders were in effect at all times relevant to this action. (Recommended Order at 3).

B. Respondents' Notice of Special Meeting.

In July 2016, Respondents hired David Harper, a Louisville attorney, to reconstitute the Bank's board of directors. (Hearing Transcript, p. 100). As explained in the Recommended Order, "Harper advised [Respondents] that he believed the shareholders could elect new directors in spite of the provisions of the Consent Orders, based on a federal regulation, 12 CFR 303.102(c)(2), which provides for an "automatic waiver" of a 30-day waiting period for directors to take office, contained in an earlier portion of the same regulation. (Hearing Transcript, p. 74)." (Recommended Order at 3).

Harper prepared a July 29, 2016 Notice of Special Meeting of Shareholders, which DFI received from then-Bank President Kevin Mullins. (DFI's Hearing Exhibit 3; Hearing Transcript, p. 83). The Notice stated that the shareholder meeting, to be held on August 12, 2016, would include taking steps to: "fix as shareholders the number of directors at five (5)" and "remove the current directors of the Bank and to elect the following five (5) persons: Gallie Isaac, Jr., Kevin R. Mullins, Kathy Reid, Howard R. Sanders, Gene A. Wilson, or such of them and such other persons

as may be properly nominated and elected at the Special Meeting.” (DFI’s Hearing Exhibit 3). Commissioner Vice testified that he had not been surprised by the Notice in light of Wilson’s previous comments during the earlier board meeting regarding his intent to restructure the Board. (Hearing Transcript, p. 25). As further explained by Commissioner Vice, DFI had not received any request for approval; nor had it issued any written approval for the proposed actions to be taken at the Special Meeting. (Hearing Transcript, p. 26).

C. Reminders and Warnings against Violating the Consent Orders.

1. August 5, 2016 Joint Regulatory Letter.

The Recommended Order correctly notes that Commissioner Vice and M. Anthony Lowe, FDIC regional director, jointly sent a letter to the board of directors on August 5, 2016. (DFI’s Hearing Exhibit 4) (Recommended Order at 5). The letter advised the board that the Bank was in a troubled condition and had to abide by Section 32 of the Federal Deposit Insurance Act and Subpart F of Part 303 of the FDIC Rules and Regulations. (Id.) The letter also reminded the board that, in addition to the foregoing FDIC rules, the Bank was also operating under existing Consent Orders, which contained provisions pertaining to management and the composition of the board of directors. The correspondence further warned of possible civil monetary penalties and the potential removal of board members in the event of noncompliance with the Consent Orders. (Id.)

2. Letter from the Bank’s Attorney.

The Hearing Officer also correctly found that James Moore, the Bank’s attorney, submitted a letter to the Bank’s board on August 11, 2016. (DFI’s Hearing Exhibit 5) (Recommended Order at 5). Moore’s letter reminded the directors that the Bank was under Consent Orders, and that the proposed actions outlined in the Notice of Special Meeting of Shareholders would violate those

Orders, thereby potentially subjecting the board and others “to the imposition of significant civil monetary penalties and fines.” (DFI’s Hearing Exhibit 5).

3. Regulators’ Separate Letters and Personal Appearances at Bank’s August 11, 2016 Board Meeting.

Commissioner Vice, Ralph Crisp, then an examiner with DFI, and Dan Malone, Assistant Regional Director of FDIC, attended a regularly scheduled board meeting of the Bank on August 11, 2016, one day before the date scheduled for the Special Meeting of Shareholders. (Hearing Transcript, p. 29). There, Commissioner Vice read another letter, dated August 11, 2016, to the members of the board, once again reminding the Bank, and its institution-affiliated parties, that the Bank was under Consent Orders which prohibited adding members to the Board without prior written approval from DFI and FDIC. (DFI’s Hearing Exhibit 6) (Recommended Order at 5). The letter also informed the board that neither DFI nor FDIC had issued written approval for the changes proposed in the meeting notice and reiterated that the Amended Consent Order obligated the Bank and its institution-affiliated parties to maintain a Board composed of at least five Directors with at least 2/5 of the members to be independent. Finally, the correspondence warned the Board, which included Respondents, of civil penalties under KRS 286.3-990(15) for violations of the existing Consent Orders. (Id.)

Commissioner Vice testified at the hearing that, through his presence at the Bank’s board meeting, he wanted to make sure that the Bank understood the importance of the letter and the ramifications for failing to follow the provisions of the Consent Orders. He therefore personally read the letter to the Bank directors in its entirety, and left a copy with them. (Hearing Transcript, p. 30). Commissioner Vice individually asked each Board Member in attendance if they understood the letter. Respondent Wilson responded that he did not necessarily agree with the letter, but that he did understand it. (Hearing Transcript, p. 31) (Recommended Order at 5).

Similar to Commissioner Vice, Dan Malone of the FDIC also read a prepared letter with the same message at the meeting; confirmed each director in attendance understood it; and offered to answer any questions they might have. (Hearing Transcript, p. 31).

4. Commissioner Vice's Telephone Call with David Harper.

In addition to the foregoing letters and personal visit, Commissioner Vice also had a telephonic conversation with Respondents' then-attorney David Harper on August 12, 2016, the day of the Special Meeting of Shareholders. (*Id.*) (Recommended Order at 6). During the call, Commissioner Vice again reminded Harper that the Bank and its institution-affiliated parties, including shareholders who participate in the conduct of the affairs of the Bank, were bound by the Consent Orders, which required written approval from FDIC and DFI before any member could be added to the Bank's board of directors. (Hearing Transcript, p. 32). Harper disagreed, asserting that a 30-day waiver found in FDIC Regulation 303 could be used to reconstitute a board. In response, Commissioner Vice informed Harper that this was incorrect, and that the outstanding Consent Orders would supersede the regulation referenced by Harper. (Hearing Transcript, p. 32) (Recommended Order at 6).

D. August 12, 2016 Special Meeting of Shareholders.

The Hearing Officer found that, despite the reminders and warnings from the regulators, the August 12, 2016 Special Meeting occurred as the shareholders planned. The Recommended Order noted that the shareholders removed the existing board of directors and elected a new five-member board which consisted of three holdover members, Wilson, Reid, and Roger Smith, along with two new members, Howard Sanders and Pauletta Wilson, who is the wife of Respondent Gene Wilson. (DFI's Hearing Exhibit 7) (Recommended Order at 5). The Hearing Officer also found that, "[u]nless legally excused for some reason, this action clearly violated the first Consent

Order, requiring approval from KDFI and FDIC before electing any new members.” (Recommended Order at 5).

E. Aftermath of the Special Meeting of Shareholders.

1. Communications between Harper and DFI/FDIC.

Following the shareholder meeting, Harper sent DFI and FDIC a letter dated August 16, 2016 detailing what had occurred. (DFI’s Hearing Exhibit 10). In response, FDIC sent a letter dated August 17, 2016 to the Bank’s board of directors, acknowledging receipt of Harper’s letter and again reminding the Board that they were under joint Consent Orders with DFI and FDIC. (DFI’s Hearing Exhibit 11). The letter advised that the Bank “must receive written approval from the FDIC and the KDFI before Mr. Sanders and Ms. Wilson can assume their duties as Directors on the Bank’s board.” (*Id.*) The letter also pointed out that Harper’s August 16 submission “did not reference or request permission under the Joint Consent Order for Mr. Sanders or Ms. Wilson to assume responsibilities to serve as Directors.” (*Id.*)

The Hearing Officer further noted that Harper spoke by telephone with a Mr. Divis at the FDIC in Chicago. Harper testified that Mr. Divis told him that they had a legitimate five-member board (although neither was aware that Roger Smith would decline to serve), but that the two new members should not vote until they had been approved by the FDIC. (Recommended Order at 6).

2. “New Board” Meets and Conducts Business.

On August 17, 2016, the newly-elected Board (“New Board”) held a meeting. According to the meeting minutes, four directors were present: Respondents Wilson and Reid (by telephone), and the two recently added, Mr. Sanders and Ms. Wilson. The minutes indicate that the four directors “took and gave the required oath” and conducted business on behalf of the Bank. (DFI’s

Hearing Exhibit 12). Respondents stipulated at the hearing that the New Board had, in fact, met and conducted Bank business. (Hearing Transcript, p. 44).

On August 25, 2016, Roger Smith sent a letter to DFI and FDIC indicating that, although he had been elected to serve on the Board of Directors at the special meeting, he was not interested in serving “on the new board.” He asked, instead, that Kevin Mullins be elected to replace him. (Hearing Transcript, p. 39). Smith subsequently sent a letter dated August 29, 2016, which stated that he had submitted his resignation from the Board of Directors effective August 26, 2016. (DFI’s Hearing Exhibit 9). In light of this occurrence, the Hearing Officer ruled that “(again, absent some legal excuse), the Respondents were in violation of the Amended Consent Order (and KRS 286.3-040) by having only four members on their board, after Mr. Smith declined his election.” (Recommended Order at 6).

3. Lawrence County Lawsuit.

Despite the numerous aforementioned warnings from regulators, the reconstituted board continued to do business in the name of the Bank. On September 26, 2016, the members of the Bank’s board of directors who had been removed through the vote held at the Special Meeting of Shareholders (the “Old Board”) filed suit against the New Board in Lawrence Circuit Court. Judge C. David Hagerman, acting as Special Judge in Lawrence Circuit Court, entered an Order Granting a Temporary Injunction on October 6, 2016. (DFI’s Hearing Exhibit 13). The Order specifically stated that Wilson and Reid must comply with any and all FDIC and DFI requirements involving removal and election of board members, “including but not limited to any and all requirements and restrictions contained in the Consent Orders, letters, and Notice of Assessment of Fines from the FDIC and KDFI...” (Id.)

The Order also “prohibited” Wilson and Reid “from promoting, nominating or electing any new member of the Bank’s Board of Directors unless or until specific written approval has been obtained from the FDIC and KDFI for that individual to serve as a member of the Bank’s Board of Directors in accordance with the Consent Orders.” (Id.) These findings were made permanent by Judge Hagerman on May 18, 2017, through his Order granting the Old Board’s Motion for Judgment on the Pleadings, finding that the prior members were not legally removed as Bank directors during the August 12, 2016 shareholders meeting “because of regulatory prohibitions on the appointment of new directors contained in the Consent Orders.” (May 18, 2017 Order (DFI’s Post-Hearing Brief, Exhibit 1) at p.1, ¶(b) (emphasis added).

In the Recommended Order, the Hearing Officer recognized that the “Temporary Injunction was made permanent by a Judgment of the Lawrence Circuit Court on May 18, 2017,” but found that “the Respondents have appealed this Judgment to the Kentucky Court of Appeals, and therefore it is not final.” (Recommended Order at 7). Because it is determined in this Final Order, based on controlling case law, that the pendency of an appeal does not affect the finality of a judgment for purposes of issue preclusion, the Hearing Officer’s foregoing finding on “finality” is erroneous and will be amended herein as set forth below.

CONCLUSIONS OF LAW

The Recommended Order observed that “[t]here are two primary legal questions in this matter. First, does the automatic waiver provision of 12 CFR 303.102(c)(2) operate to allow the shareholders of a bank to appoint new directors in contravention of a Consent Order, such as was in effect in this case? Second, does the good faith of the Respondents, or their reliance on the advice of counsel, relieve them of the possibility of sanctions for violating a Consent Order, into which they personally entered?” (Recommended Order at 7-8). The Hearing Officer analyzed

those questions, and correctly answered both in the negative. For the following reasons, such rulings are hereby affirmed and adopted as final.

A. Adoption of Hearing Officer’s Recommended Conclusions of Law.

1. 12 CFR 303.102(c)(2) does not provide a waiver of the requirements of the Consent Orders.

The Recommended Order noted that “it is apparent from the language of both the regulation and the Consent Orders that at least in this case,” 12 CFR 303.102(c)(2) does not provide a waiver of the requirements of the Consent Orders. (Recommended Order at 8). The Hearing Officer correctly found that that the federal regulation’s “automatic waiver” provision relied on by Respondents waives only the notice requirements imposed by a prior subsection of that regulation. It does not waive, and in fact has no bearing upon, the separate and distinct obligations independently created by the voluntary Consent Orders. (Id.)

In particular, subsection (a) of the regulation, among other things, requires a bank in a troubled condition to “give FDIC written notice . . . at least 30 days prior to adding or replacing any member of its board of directors.” 12 CFR 303.102 (a). The “automatic waiver” provision actually appears in subsection (c)(2) of that regulation and, under certain circumstances, provides for the waiver of the prior notice requirements imposed upon a bank under the aforementioned subsection (a). It specifically states that “in the case of the election of a new director not proposed by management at a meeting of the shareholders . . . the prior 30-day notice is automatically waived and the individual may begin serving” 12 CFR 303.102(c)(2). Thus, the very terms of the regulation demonstrate the restriction of the waiver’s applicability to the regulation’s own requirements. Indeed, while the regulation makes no mention of other sources of obligations, it expressly discusses a “prior notice provision.” The Consent Orders issued here, on the other hand, do not reference “notice,” but rather require actual prior “approval.” (DFI’s Hearing Exhibit 1 at

3; DFI's Hearing Exhibit 2 at 2-3). Expressly highlighting these distinctions between a waiver of the "notice" requirement in the regulation, and the "approval" requirement in the Consent Orders, the Hearing Officer correctly found that the waiver provision of the regulation simply did not apply. (Recommended Order at 9). This logical and well-reasoned finding is affirmed and adopted herein.³

2. Purported "good faith" and "reliance on advice of counsel" does not excuse Respondents' conduct.

Addressing the next legal issue, the Hearing Officer observed that the "second question is whether the fact that the Respondents acted throughout in what they believed to be the best interests of the bank, and on the advice of counsel that what they did was legally permissible, shields them from sanctions for violating the Consent Orders. It does not." (Recommended Order at 9) (emphasis added). Significantly, the Hearing Officer noted that there is no *mens rea* requirement found in KRS 286.3-990(15), the penalty statute for the allegations contemplated by this administrative action. (Id.)

³ Though not expressly addressed in the Recommended Order, inherent in its proposed findings is the proper rejection of Respondents' contention that they should be absolved of liability because they were not acting in their capacities as directors, but rather as shareholders, when they restructured the board of directors in the absence of prior regulatory approval. Respondents' assertion was based on the waiver in 12 CFR 303.102(c)(2) of its previously enumerated notice requirement "if the new director is elected directly by shareholders without being proposed by management." (Id.) (emphasis added). The record is undisputed that Wilson and Reid were directors of the Bank and, according to its bylaws, the Bank is managed by the board of directors. Accordingly, because Respondents were directors and therefore members of management, this federal regulation simply cannot be utilized to excuse Respondents' Consent Order violations. Notably, moreover, regardless of whether they are ultimately considered shareholders or directors, because Respondents constitute "institution-affiliated parties," they are ultimately bound by the Consent Orders. The original Consent Order is binding upon "the Bank [and] its institution-affiliated parties" and refers to 12 U.S.C. § 1813(u) for the definition of "institution-affiliated party," which includes "any director, officer, employee, or controlling stockholder," as well as "any shareholder...who participates in the conduct of the affairs of an insured depository institution." (DFI's Hearing Ex. 1 at 2, 20) (emphasis added). There can be no dispute that Wilson and Reid were serving as Bank directors upon the entry of the 2104 Consent Order and that they were also "significantly large shareholders" of the Bank. (Hearing Transcript, p. 81). Moreover, the overall conduct of Respondents, including their engagement of an attorney to assemble shareholders to replace the entire board of directors, plainly demonstrates their "participat[ion] in the conduct of the affairs" of the Bank. Accordingly, whether referred to as active shareholders or directors, Respondents clearly qualify as "institution-affiliated parties" bound by the terms of the Consent Orders.

In further support of its finding, the Recommended Order cited the Kentucky Court of Appeals case Flint v. Executive Branch Ethics Commission, 981 S.W.2d 132 (Ky. App. 1998), which held in another administrative action that “the statute does not require the offender to ‘knowingly’ violate the code in order to be punished under it.” (Id.) Rejecting Respondents’ assertions, the Hearing Officer determined that Wilson and Reid did in fact act “knowingly,” and that they were arguing merely that they acted on the advice of counsel. While the Hearing Officer found that there was no evidence that the Respondents acted in bad faith, “they knowingly violated the Consent Orders, nonetheless.” (Recommended Order at 10) (emphasis added). In this regard, the Recommended Order determined that after signing the Consent Orders on behalf of the Bank, Respondents violated them by (a) voting on the board reconstitution at the August 12, 2016 shareholder meeting, after being warned by regulators not to do so; and (b) continuing to meet and act on behalf of the bank with only four directors (and two voting directors) after Mr. Smith declined his election to the board. (Id.)⁴

Finally, the Hearing Officer correctly concluded that “advice of counsel” is not a valid defense in an administrative case such as the current one. (Id.) In a Kentucky Supreme Court case rejecting an advice of counsel defense in an administrative action, the Commissioner of the Department of Insurance was alleged in Executive Branch Ethics Comm’n v. Stephens, 92 S.W.3d

⁴ This Final Order accepts and adopts the Hearing Officer’s recommended finding that, in addition to appointing new board members without the required prior approval from regulators, Respondents also violated terms of the Consent Orders and Kentucky statutory law (KRS 286.3-040) by failing to maintain a board composed of at least 5 directors. (Recommended Order at 6, 10). Rejecting Respondents’ contentions relating to this portion of the claim, the Hearing Officer determined that no documents existing within the administrative record substantiate or verify Respondents’ assertions. Accordingly, based on that record, the Recommended Order’s finding of such a violation is sufficiently supported. (Id. at 6); see also KRS 13B.080 (directing that “[i]n an administrative hearing findings of fact should be based exclusively on the evidence in the record”). Notably, moreover, even if the arguments offered by Respondents had been supported by documents properly set forth in the record, they would nevertheless be found to be unavailing under the facts of this matter. Finally, even absent a finding of a violation on these grounds, because both Consent Orders combine together to impose a continuing, unified set of requirements upon the Bank, Respondents’ undisputed and unexcused acts of adding board members in the absence of prior regulatory approval, in the manner set forth above, would exclusively and independently support the fine amounts imposed herein.

69 (Ky. 2002), to have used his influence to be appointed deputy liquidator for an insurance company. In defense of that action, the Commissioner argued that he accepted the position only after being advised by counsel that it would not be illegal. Rejecting this contention, however, the Court in Stephens expressly stated that “[r]eliance on advice of counsel is not a viable defense in this action.” Id. at 74 (Recommended Order at 10). Similarly, because it is also not a viable defense to the claims at issue here against Respondents, the Hearing Officer’s conclusion of law with respect to the advice of counsel defense is affirmed and adopted in this Final Order.

3. Hearing Officer’s recommended fine amounts against Respondents will also be adopted.

Based upon his findings and conclusions, the Hearing Officer recommended that Respondents be found to have violated the terms of the regulatory Consent Orders and be penalized through a fine of \$2,100 due from each Respondent. In consideration of the relevant factors set forth in KRS 286.3-990(15), and the overall circumstances of this action, this recommended fine amount is sufficiently supported and is hereby adopted as part of this Final Order.

KRS 286.3-990(15) directs that “[i]n determining the amount of the fine the commissioner shall consider the financial resources and good faith of the . . . person charged, the gravity of the violation, the history of previous violations and such other factors as justice requires.” The record in this matter is uncontroverted that:

- As far back as December 2015, Respondent Wilson was discussing his plan to restructure the board by reducing the number of board members to five and appointing new directors per his personal preference (Hearing Transcript, p. 23);
- By virtue of their being signatories to the Orders as Bank directors, Respondents, and the other members of the board, expressly obligated the Bank and its affiliated officials to abide by the terms of the Consent Orders the Respondents subsequently violated (DFI’s Hearing Exhibit 1 at 20; DFI’s Hearing Exhibit 2 at 11);

- In ignoring the requirements of the Orders, Respondents took part in effectuating the precise board restructuring that Wilson had been previously proclaiming (Hearing Transcript, p. 23);
- Frequent warnings in the form of letters, in-person discussions, and phone calls were provided to Respondents and their counsel by members of DFI, FDIC and the Bank's own attorney (Complainants' Post-Hearing Brief, p. 5-8); and
- Respondents were repeatedly warned that the actions they were considering, and ultimately took, would constitute significant violations resulting in the very fines at issue in this matter. (Id.)

Indeed, the evidence shows that Commissioner Vice and Dan Malone of FDIC, with their repeated reminders and warnings, did everything they could to avoid having to penalize the Bank or any of its institution-affiliated parties. They simply wanted the Bank directors and members to abide by the Consent Orders, which were put in place to correct extreme deficiencies in the Bank's oversight and management. However, despite these regulatory efforts, Respondents just refused to comply.

Moreover, by virtue of the Respondents' "knowing" violations of the regulatory Consent Orders (see Recommended Order at 10), the Bank itself was originally named in this action and agreed to pay a fine for its violations as part of its settlement with the Department. Respondents' actions also led to a lawsuit being brought against the Bank and its "New Board" in Lawrence Circuit Court by members of the Bank board who were displaced through the actions orchestrated by Respondents. This lawsuit, which remains ongoing, has cost, and continues to cost, the Bank considerable funds in legal fees and related expenses. It further creates an atmosphere of confusion and uncertainty that does little to encourage investment and confidence in the Bank. The fact that all of this was avoidable and occurred as a direct result of defying the repeated warnings and instructions of regulators engaged in supervising the activities of a "financially troubled" institution, further supports the reasonableness of the imposed fine amounts. Finally, given their

standing among the largest shareholders of the Bank and their net worth as last reported to the Bank, the \$2,100 fine per each Respondent is far from excessive or unduly punitive in consideration of their financial resources.

While this Final Order fully adopts the Hearing Officer's recommended total final amount, it amends slightly the Recommended Order's allocation method. Specifically, the Hearing Officer recommended fine amounts as delineated by enumerated violations of each separately entered Consent Order (recommending each respondent "pay \$250 for violation of the of the first Consent Order and each pay \$1850.00 (\$50.00 per day for 37 days) for violation of the second Consent Order)." (Recommended Order at 11). However, because the Consent Orders merged together to simultaneously place the Bank under the provisions of both (Hearing Transcript, p. 21), and the Bank was in violation of the merged requirements of both Orders for the 37 days identified in the Recommended Order, this Final Order allocates the total fine of \$2,100 per Respondent to be comprised of: (a) \$250.00 for their statutory violations of KRS 286.3-040 (failing to maintain a board composed of at least (5) directors); and (b) \$1,850.00 (\$50.00 per day for 37 days) for their aforementioned violations of the merged requirements of the 2014 and 2016 regulatory Consent Orders.⁵ As noted above, this allocation leaves undisturbed the total fine amount recommended by the Hearing Officer which, in light of the relevant factors, is logical, reasonable and sufficiently supported by the record.

⁵ This calculation of 37 days constitutes the time between the date of service of DFI's Notice of Assessment of Fines and the date of the issuance of the Lawrence Circuit Court's Temporary Restraining Order.

B. Modification of a Portion of Hearing Officer’s Recommended Conclusions of Law.

- 1. Contrary to the Hearing Officer’s ruling, the doctrine of issue preclusion does apply to preclude Respondents’ attempts to re-litigate the issues regarding violation of the Consent Orders and the automatic waiver provision of the federal regulation.**

Despite its agreement with, and adoption of, the majority of the Hearing Officer’s Recommended Order, this Final Order disagrees with, and hereby modifies, the Hearing Officer’s erroneous finding that the Lawrence Circuit Court Judgment is not final, for purposes of the issue preclusion doctrine, because the case is pending on appeal. Specifically analyzing whether the Circuit Court judgment operates as issue preclusion so as to bar re-litigation of Respondents’ arguments based on the automatic waiver provision, the Recommended Order found that “Respondents have appealed the Lawrence Circuit Court’s Judgment, and that appeal is pending. Therefore, the Judgment is not final, and the doctrines of *res judicata* and issue preclusion do not apply.” (Recommended Order at 8). Because this statutory interpretation errs as a matter of law and, if adopted, could create misleading and misguided precedent, it is overruled and modified as set forth herein.

The Kentucky Supreme Court has long recognized the doctrine of issue preclusion which, under certain circumstances, bars a party from raising an issue that has already been litigated. Discussing the applicability of the doctrine in Coomer v. CSX Transp., Inc., 319 S.W.3d 366 (Ky. 2010), the Court observed that “[f]or issue preclusion to apply, four elements are necessary: (1) the issue must be identical in both cases; (2) the issue must have been actually litigated; (3) the issue must have been actually decided; and (4) the issue must have been necessary to the court’s judgment.” Coomer, at 374.

Given the portions of the Circuit Court’s final Order previously cited herein, and the bases for the fines at issue in the current matter, it is clear that central to the dispositions of both matters is the question of whether Respondents’ reconstitution of the Bank’s board of directors violated the regulatory Consent Orders. Indeed, this issue serves as the crux of the current administrative action, and it was litigated and decided in the Circuit Court case, constituting the primary and fundamental holding of Judge Hagerman’s dispositive Order. Accordingly, Respondents’ violations of the Consent Orders have been established as a matter of law.

It is undisputed that Lawrence Circuit Court ruled that the reconstitution of the Board was unlawful because it violated the Consent Orders. In that action, the Court considered Wilson and Reid’s defense of reliance on 12 CFR 303.102. In fact, Respondents’ Post-Hearing Brief indicated that “[t]he precise issue here was also presented to Judge David Hagerman...” in the Lawrence Circuit Court action. Wilson and Reid also stated in their brief that their “right to avail themselves of the authority granted by 12 U.S.C. §303.102(c)(2) was at issue in both the case before Judge Hagerman and now on appeal.” (Respondents’ Post-Hearing Brief, p. 4).

Moreover, the fact that the Lawrence Circuit Court Judgment is on appeal has no bearing on the finality of the judgment for purposes of issue preclusion. It is well-settled that the “pendency of an appeal does not destroy finality of judgment for the purposes of issue preclusion under Kentucky law.” Stemler v. City of Florence, 126 F.3d 856, 871 (6th Cir. 1997); see also Roberts v. Wilcox, 805 S.W.2d 152, 153 (Ky. App. 1991) (following the “long-standing federal rule” which “hold[s] that the pendency of an appeal has no effect whatsoever on the finality of a judgment for purposes of collateral estoppel”).

The finality requirement for issue preclusion was specifically analyzed in a recent federal case applying Kentucky law and addressing facts remarkably analogous to the instant case. In

Preferred Care of Delaware, Inc. v. Quarles, 5:15-CV-177-TBR, 2016 WL 3562123 (W.D. Ky. June 24, 2016), aff'd sub nom. Preferred Care of Delaware, Inc. v. Crocker, 16-6179, 2017 WL 3223003 (6th Cir. Feb. 28, 2017), a party tried to litigate the validity of an arbitration agreement in federal court after the Trigg Circuit Court had ruled the agreement to be invalid. In addition to the federal action, the party had appealed the Trigg Circuit Court ruling to the Kentucky Court of Appeals. The Court in Quarles, in ruling that the party was, in fact, precluded from re-litigating the arbitration issue, stated as follows:

The only element at issue here is whether or not the validity of the parties' Arbitration Agreement has been "actually decided" in the state court action. The Trigg County Circuit Court issued its order finding the Arbitration Agreement invalid on December 17, 2015. Subsequently, on January 11, 2016, the Plaintiffs in this action appealed the circuit court's adverse decision to the Kentucky Court of Appeals. The Plaintiffs' appeal is still pending before the Kentucky Court of Appeals. As their appeal of the circuit court's adverse decision is still pending, the Plaintiffs argue that the circuit court's order does "not meet the standard for finality for [issue preclusion] purposes." However, under Kentucky law, "the pendency of an appeal does not destroy the finality of the [circuit court's order] for the purposes of issue preclusion." *Epps Chevrolet Co. v. Nissan N. Am., Inc.*, 99 F. Supp. 3d 692, 701-02 (E.D. Ky. 2015) (quoting *Stemler v. City of Florence*, 126 F.3d 856, 871 (6th Cir. 1997)).

Quarles, at 3 (additional internal citations omitted) (emphasis added).

Similarly here, it is undisputed that the exact issues in the current case were litigated and decided in the Lawrence Circuit Court action. Consistent with the uniform holdings of the foregoing authority, Judge Hagerman's ruling was a final judgment for issue preclusion purposes, regardless of the pending appeal. Accordingly, because Respondents' violations of the Consent Orders have been established as a matter of law, and cannot be revisited, the Hearing Officer's recommended finding to the contrary is modified as set forth herein.

FINAL ORDER

THEREFORE, based on the foregoing findings of fact and conclusions of law, and pursuant to KRS 286.3-690, KRS 286.3-990(15), and KRS 13B.120, IT IS HEREBY **ORDERED** AS FOLLOWS:

1. Respondent, Gene A. Wilson, shall pay a fine of a fine of \$2,100 for violations of the regulatory Consent Orders and statutes as set forth herein. Payment of this fine shall be due on or before February 19, 2018.

2. Respondent, Kathryn Reid, shall pay a fine of a fine of \$2,100 for violations of the regulatory Consent Orders and statutes as set forth herein. Payment of this fine shall be due on or before February 19, 2018.

This is a **FINAL AND APPEALABLE ORDER**. The **EFFECTIVE DATE** of this Order shall be the date reflected on the certificate of service attached to this Order.

NOTICE OF APPEAL RIGHTS

Pursuant to KRS 286.3-690, you are hereby notified that any person aggrieved by this Final Order of the Deputy Commissioner may obtain a review of the Order by the Lawrence Circuit Court. If you choose to appeal, you must file a written petition asking for review within thirty (30) days after the date reflected on the certificate of service attached to this Final Order. A copy of the petition must be served upon the Commissioner.

SO ORDERED this 17th day of February, 2018.



BRIAN H. RALEY
DEPUTY COMMISSIONER

Certificate of Service

I hereby certify that a true and correct copy of the foregoing **Final Order** was entered by the Deputy Commissioner and sent by certified mail, return receipt requested, on this the 17th day of JANUARY, 2018, to:

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Counsel of Record for Respondent

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State Government Messenger Mail to:
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Executive Director
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