OFFICIAL TRANSCRIPT

PROCEEDINGS BEFORE

THE SUPREME COURT

OF THE

UNITED STATES

CAPTION: BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM OF THE UNITED STATES, Petitioner, V. MCORP FINANCIAL, INC., ET AL.;

and

MCORP, ET AL., Petitioners V.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM OF THE UNITED STATES

CASE NO: 90-913; 90-914

PLACE: Washington, D.C.

DATE: October 7, 1991

PAGES: 1 - 45

ALDERSON REPORTING COMPANY

1111 14TH STREET, N.W.

WASHINGTON, D.C. 20005-5650

202 289-2260

IN THE SUPREME COURT OF THE UNITED STATES

- - - - - - - - - - - - - - - - - - - -X

BOARD OF GOVERNORS OF THE :
FEDERAL RESERVE SYSTEM OF THE :
UNITED STATES, :
Petitioner :
v. : No. 90-913
MCORP FINANCIAL, INC., ET AL. :

- - - - - - - - - - - - - - - - - - - -X

MCORP, ET AL., :
Petitioners :
v. : No. 90-914
BOARD OF GOVERNORS OF THE :
FEDERAL RESERVE SYSTEM OF :
THE UNITED STATES :

- - - - - - - - - - - - - - - - - - - -X

Washington, D.C.

Monday, October 7, 1991

The above-entitled matter came on for oral argument before the Supreme Court of the United States at 11:07 a.m.

APPEARANCES:

JEFFREY P. MINEAR, ESQ., Assistant to the Solicitor General, Department of Justice, Washington, D.C.; on behalf of the Federal Reserve System.

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

APPEARANCES: (continued)

ALAN B. MILLER, ESQ., New York, New York; on behalf of MCorp, et al.

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

CONTENTS

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

PROCEEDINGS

(11:07 a.m.)

CHIEF JUSTICE REHNQUIST: We'll hear argument now in No. 89-913, Board of Governors of the Federal Reserve System of the United States v. MCorp Financial, Inc.

Mr. Minear, you may proceed.

ORAL ARGUMENT OF JEFFREY P. MINEAR

ON BEHALF OF THE FEDERAL RESERVE SYSTEM

MR. MINEAR: Thank you, Mr. Chief Justice, and may it please the Court:

This case arises from the Federal Reserve Board's attempts to regulate MCorp, a Texas-based bank holding company that is operating in bankruptcy as debtor in possession. The basic issue is whether a district court sitting in bankruptcy may enjoin the Federal Reserve Board from conducting a proceeding to determine whether MCorp is engaging in unsafe and unsound practices. That issue turns on the meaning of Section 1818 of the Financial Institutions Supervisory Act, also known as FISA.

Section 1818, subsection (b), provides that the Federal Reserve Board may initiate a proceeding like the one involved here to investigate a bank holding company's practices and to issue, if necessary, a cease-and-desist

order. Subsection (h) further provides that an aggrieved party make seek judicial review of any such order accord -- in accordance with the Administrative Procedure Act.

Subsection (i) then states as follows, and I quote, "Except as otherwise provided in this section, 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."

We submit that Section 1818(i) means what it says, and it prohibits any court, including a district court sitting in bankruptcy, from interfering with the Board's ongoing proceedings.

QUESTION: Now Congress -- suppose the district court hadn't done anything except to say -- except to remind the Board that the statute says that there's an automatic stay of all proceedings.

MR. MINEAR: Yes, Your Honor, the Bankruptcy Code does provide an automatic stay. It also provides an exception to the automatic stay. And if I may read that to you as well, I think it clarifies the stay is not applicable here. It states that the automatic stay does not apply to, and I quote, "the commencement or continuation of any action or proceeding by governmental unit to enforce such governmental unit's police or

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

regulatory power."

QUESTION: Does that apply to everything that the Board was doing?

MR. MINEAR: Well, it certainly applies to an action to cease and desist an unlawful practice, and that is what the Board has asserted here.

QUESTION: The lower court's ruling was not based on the automatic stay provision.

MR. MINEAR: That is correct. It did not even reach that issue, and it rejected all of MCorp's bankruptcy allegations. The court of appeals, in fact, largely agreed with our construction of Section 1818(i), that it would prohibit any such proceeding in the bankruptcy court in accordance with bankruptcy law. It further held, however, that this Court's decision in Leedom v. Kyne, provided the court with inherent jurisdiction to enjoin the Board's proceedings.

Now we have petitioned this Court to review the Leedom holding, while MCorp has petitioned on the bankruptcy law issues. And I would like to begin by addressing the question of Leedom, which has been a continuing source of confusion for the lower courts.

Leedom arose out of a dispute before the National Labor Relations Board over a certification of a bargaining unit for certain Westinghouse professional

employees. The labor act did not expressly provide for judicial review under the facts of that case. This Court held, however, that a judicial review action could proceed notwithstanding the absence of any particular judicial proceeding that was specified by statute. It reasoned that a cause of action could be inferred because the absence of jurisdiction under the specific facts there would amount to the obliteration of congressionally conferred right.

This Court has described Leedom as a narrow and painstakingly delimitated decision. And whatever the wisdom of Leedom under its specific facts, it has no application to a case such as this.

First, here, unlike in Leedom, there has been no agency decision. Rather, this case is like FTC v. Standard Oil. The agency has simply begun the process of making its decision by providing a notice of charges.

Second, and again unlike in Leedom, Congress has expressly provided that an aggrieved party will be entitled to judicial review once the agency actually makes its decision.

And third, again unlike in Leedom, Congress has expressly foreclosed all other judicial remedies. In short, Congress has carefully considered the question of appropriate judicial relief.

QUESTION: Mr. Minear, could I ask you whether under FISA the Board is ever able to compel the bank holding company to spend its assets to take care of the subsidiary banks before an Article III court has had a chance to review the Board's order?

MR. MINEAR: Has it ever done so or can it do so?

QUESTION: Is it possible under the law that the Board can compel that transfer of assets before a court has had a chance to review it?

MR. MINEAR: It could issue an order, but that order would immediately be subject to judicial review.

QUESTION: It's immediately subject to appeal and judicial review.

MR. MINEAR: Yes, and the Board --

QUESTION: And the minute that happens, is it also theoretically possible then, that a bankruptcy court could have jurisdiction?

MR. MINEAR: That point might be debatable. One point, to clarify as to the first point that you made. The -- an order from the Board will not be effective for 30 days from the point of issuance, so that provides a 30-day window to seek judicial relief.

The second question you raised was whether a bankruptcy court would be able to review that. Under FISA

Section 1818(h), a court of appeals is vested with the jurisdiction to review the orders of the Board. I suppose it's a possible argument that the bankruptcy court might have authority to review it under 1334(b).

QUESTION: Wouldn't you then get the priority section under the Bankruptcy Code if somebody went to the bankruptcy court and said, look, now we're here, and couldn't they apply their jurisdiction at that stage?

MR. MINEAR: Well, first of all, this is not a claim in bankruptcy as you might -- arise from a debtor. MCorp is not being obligated to pay any money at all to the Federal Reserve Board. Rather, it's been required --

QUESTION: It could happen, presumably.

MR. MINEAR: That MCorp could be required to pay money to the Fed?

QUESTION: No, no, no, no. That you could have this overlapping jurisdiction in a given situation, if the funds were ordered transferred.

MR. MINEAR: It could be that there would be overlapping jurisdiction at some point, but I think that question, of course, is premature here. All we seek to do is go forward with our proceeding. I think it's a debatable point whether the bankruptcy court would, in fact, have -- concurrent jurisdiction in that situation. It would depend in part on whether the order affected --

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

was related to, the case -- a case under Title XI, I think. And it would also depend on the scope with the preclusive effect of Section 1818(i).

QUESTION: Do you think there are any limits on the authority of the Board to determine what's an unsound banking practice and to the relief that it can order?

MR. MINEAR: Oh, certainly there are limits, but nevertheless, Congress has not defined that term. And the Board is entitled to make a reasonable judgment on this, and its views are entitled to deference.

QUESTION: And has the Board been consistent in its view of its power?

MR. MINEAR: On this particular question, yes it has. As with respect to unsafe and unsound practices, that opens up a broad array of possible forms of mismanagement that might arise.

QUESTION: You want to get Leedom, but while we're on Justice O'Connor's question, assume that the Board conducts its proceedings, issues its orders, and there is then an appeal to the circuit court which ratifies the Board's order. At that point, there is an order to MCorp to transfer property to subsidiary banks. At that point does 1334(d) come into effect so that the bankruptcy court then has jurisdiction to review the propriety of that order transferring property?

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

MR. MINEAR: Well, 1334(d) gives the bankruptcy court exclusive jurisdiction over the property of the debtor. Again, we have to speculate here on what might happen, if I can follow the course that you've laid out. If the order has been approved, the first thing -- has been subject of judicial review and has been upheld, the first question would be the content of that order. Now it might be that the order will simply direct MCorp to put together a plan for providing capital to its subsidiary banks.

If MCorp is subject to such an order, I assume that it would go to the bankruptcy court and seek such relief, that this is outside the ordinary course of business. MCorp could provide money to its subsidiaries, provided it falls within 363(c) of the Bankruptcy Code, but it's a matter within the ordinary course of business. Assuming it's not, MCorp would go to the bankruptcy court and seek approval of its plan to comply with the Board's order. But the Board's order should simply be treated as a law that MCorp has to apply -- has to comply with.

And as this Court indicated in the Midlantic National Bank case, simply being a debtor in possession does not exempt you from other regulatory requirement.

QUESTION: And I take it works that way under the National Labor Relations Act. If a bankrupt is

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

subject to an NLRB action, it simply goes to the circuit court, the NLRB is either -- if the NLRB is affirmed, then any property transfer is under the control of the bankruptcy court, and the bankruptcy court is simply bound by that decree.

MR. MINEAR: I believe that is the case. And there are cases such as Nathanson v. NLRB, which is a pre-code case, which indicates that the bankruptcy court should defer to the agency in terms of even liquidating back pay agreements. Now, of course, that's far down stream from where we are right now. Our question is just whether the Board should be allowed to go forward with its proceeding in this case. The Board has been completely stymied in even going forward with its administrative proceeding here.

Now as I was saying, Congress has carefully considered the question of appropriate judicial relief in this case, and that clearly distinguishes this case from Leedom. Congress has provided that MCorp will have full opportunity to seek judicial review of the Board's action once the Board definitively acts. At the same time, Congress has been quite express and explicit in stating that MCorp has no right to review at all until the Board completes its administrative investigation and determines whether it will issue an order.

Now, no such order has issued here. The Board has simply filed a notice of charges. That's all that is issue -- is at issue. As a result of the lower court's injunction, however, there is no administrative record, there has been no administrative proceeding, and it's unclear at this point what action the Board might take.

MCorp really makes no serious attempt to defend the court of appeals' Leedom rationale. In fact, its brief it devotes a mere two paragraphs to the Leedom question. MCorp argues instead that Section 1818's limitations do not apply in the bankruptcy context. And as the court of appeals stated, that is simply not so. It is important to recall the precise language of Section 1818(i): except as otherwise provided in this section, no court shall have jurisdiction to enjoin the Board's ongoing proceedings. That provision contains no exception for bankruptcy courts, and the bankruptcy law itself contains no such exception.

Now as I mentioned before, MCorp has attempted to find an exemption in the Bankruptcy Code's automatic stay provision. However, that stay is subject to an exception itself, and that exception precisely mirrors Section 1818(i). It allows the actions of the Board to go forward, notwithstanding the bankruptcy action, and it prohibits the court from -- in effect from enjoining that

type of action.

It's important to remember also that the Board initiated the proceeding here to determine when -- whether MCorp, which continues to function as a bank holding company, is in violation of the safety and soundness requirements of the Board. And as I stated before, the filing of a bankruptcy petition, in the Court -- this Court's words, does not give a debtor in possession carte blanche to ignore regulatory requirements.

Here MCorp has elected to continue in operation and continue to own banks and continue to operate banks. Thus the need for Board oversight remains. As long as MCorp continues such operations, it should be subject to the same regulatory requirements that apply to any other bank holding company in operation.

MCorp also -- attempts to find an exception to Section 1818(i) in the jurisdictional provisions of the Bankruptcy Code, as set forth at 28 U.S.C. 1334. The particular provision that MCorp relies on, however, does not continue the exception to Section 1818(i). It's no different than any of Title XXVIII's other jurisdictional provisions. They are all subject to Section 1818(i) of FISA.

MCorp relies on the fact that 28 U.S.C. 1334(b) gives a bankruptcy court jurisdiction over civil

proceedings related to a bankruptcy case. But that argument really takes MCorp nowhere. As an initial matter, all that's at issue here are administrative proceedings. Section 1334(b) does not speak to those. Second, Congress has specified exactly what civil proceeding is available for challenging the Board's order. And as I have explained, that is the petition for judicial review under Section 1818(h).

QUESTION: Excuse me. What we have here immediately is an administrative proceeding, right?

MR. MINEAR: That is correct.

QUESTION: But the attempt to review the propriety of that administrative proceeding is a civil proceeding.

MR. MINEAR: That is correct as well.

QUESTION: So you are within 1334(b). It is a civil proceeding related to a case under Title XI.

MR. MINEAR: But what is the civil proceeding, Justice Scalia? That is the civil proceeding that Congress has provided in section 1818(h), which is a petition for judicial review of a final order. There's no final order in this case. So you have jurisdiction, but you don't have a cause of action. That's really the problem here, at least under your theory under here -- under your theory of 1334(b) jurisdiction.

I mean, there has to be a cause of action against the Government somewhere. I mean, that was the -- that is one of the principal criticisms of Leedom, that it has inferred a cause of action against the Government.

QUESTION: So your argument is not an argument of one statute's superseding the other, but just of no cause of action here, at this stage, essentially.

MR. MINEAR: That is correct. There would be a cause of action once the agency acts. And again, this mirrors the APA as well. There is generally no cause of action until there is final agency action. So again you see under our theory all the pieces fit together quite nicely.

Now MCorp has also asserted that jurisdiction exists under 28 U.S.C. 1334(d), the exclusive -- which provides jurisdiction over property. And as Justice Kennedy inquired, the question there is whether there is any effect on property at this stage. And clearly, there is not. The court of appeals recognized this fact as well at page 20 and 25 of its opinion, joint appendix pages 20 and 25. The mere commencement and continuation of an administrative proceeding has no effect on property. Any effects on property will depend on what the content of the order that is issued ultimately contains.

In short, we think that the court of appeals

correctly ruled that there is nothing in the bankruptcy code that grants a district court jurisdiction to enjoin the Board's ongoing proceeding. Section 1818(i) provides that no court shall have that power, and there's no basis for making exception in the case of bankruptcy courts. That conclusion gives effect to the plain language of Section 1818(i) and avoids an inferred repeal of Congress' expressed and unqualified command.

Moreover, our position really imposes no hardship on MCorp as well. If the Court adopts our position, the injunction will be lifted; the Board's proceeding will go forward. If the Board concludes that a remedy is warranted, it may issue a cease-and-desist order, and at that point, MCorp may obtain judicial review. Thus, the only hardship that MCorp faces here is the obligation to participate in the Board's hearing. And as this Court stated in FTC v. Standard Oil, that is no legally cognizable harm. It is simply part of the social burden of living under government.

If this Court agrees with our submission that the courts below lack jurisdiction to interfere with the Board's ongoing proceedings, then there is no occasion to address the remaining question in this case: whether the Board has statutory authority to apply its source of strength as it relates to the facts here. Indeed, you'll

face that issue only if you adopt the court of appeals' Leedom analysis.

We think you should not follow that course. But if you do, then you should decide the source-of-strength issue in favor of the Board. The Board is certainly justified in treating MCorp's failure to contribute capital as an unsafe or unsound practice under the facts alleged in the notice of charges here. As this Court recognized in its Lincolnwood decision, the Board has long recognized and frequently reiterated that bank holding companies should be a source of strength to subsidiary financial institutions.

MCorp has not challenged the facial validity of that regulation. The question instead is whether MCorp's failure to comply with that regulation is an unsafe or unsound practice under FISA in the particular circumstances that are presented there. Now FISA does not define the term "unsafe or unsound practice," and the question is whether the Board's interpretation of that term is reasonable. Here the Board has reasonably concluded that a bank holding company's failure to provide financial support to its bank subsidiaries when it is able to do so can be a form of mismanagement that threatens the financial well-being of the holding company, its subsidiary, and the public.

First the holding company's failure to act as -- failure to support or refusal to support in this case its subsidiary banks can result in the wasting of an asset. If MCorp's subsidiary banks collapse because of an absence of adequate capital, the holding company's own balance sheet will be affected.

QUESTION: Mr. Minear, if we agree with you on the first point, the jurisdictional argument, is it necessary for us to go ahead and address this second question?

MR. MINEAR: Absolutely not. No. And in fact, that issue would not -- the only way this issue arises is if you adopt the Leedom analysis.

On that basis, I think that -- you know, I can restrict my comments with respect to the source-of-strength policy. As I said, it can be an unsafe or unsound practice to refuse to supply capital to subsidiary banks because it can waste the holding company's own assets. It can also result in a run on the holding company's other banks if the public is under the perception that a whole -- holding company stands behind its subsidiary banks.

And finally, of course, the public bears the cost of any of these types of failures through the provision of FDIC insurance and access to the Fed's credit

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

window. Thus, it's quite reasonable for the Fed to treat a bank holding company's refusal to aid its subsidiary banks as an -- or to treat it as an unsafe or unsound practice in the facts of this case.

The lower court's injunction has prevented the Board from conducting an evidentiary hearing, and we think the better course here is to reject the lower court's Leedom analysis and allow the administrative proceeding to go forward. But if the Court decides to reach the source-of-strength issue, it should decide it in the Board's favor.

Unless there are any questions, I will reserve the remainder of my time.

QUESTION: Thank you, Mr. Minear.

Mr. Miller, we'll hear now from you.

ORAL ARGUMENT OF ALAN B. MILLER

ON BEHALF OF MCORP, ET AL.

MR. MILLER: Mr. Chief Justice, and may it please the Court:

This morning the Government has asked the Court to overlook the fact that by statute Congress made available to bank holding companies the ability to take advantage of Title XI of the United States Code, that is to say, the Bankruptcy Code. And instead, based upon a congressional source that the Board is unable to identify,

the Board has suggested that the entire Chapter 11, proceeding under Title XI may be eviscerated by the removal of all of the assets of the holding company from the holding company to the banks while it is in Chapter 11 to leave the holding company creditors of more than half a billion dollars high and dry.

QUESTION: Well, Mr. Miller, the completion of the administrative hearing here without any enforcement beyond that won't remove any property from the holding company, will it?

MR. MILLER: It will not. However, it is our position that the orders issued by the Board in the fall of 1988, and particularly the third cease-and-desist order, which is at pages 84 and 85 of the joint appendix, go way beyond anything that the Government has represented today. That order reads, and I quote, "MCorp shall (a) take such actions as are necessary to use all of its assets to provide capital support to its subsidiary banks in need of capital, and (b) within 15 days of the effective date of this temporary order report to the Board of Governors on the identity of those subsidiary banks into which capital injections will be made by MCorp and the amount of capital to be injected into each such bank."

QUESTION: Was that order enforceable against MCorp without any further proceedings?

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

MR. MILLER: It was, Chief Justice. Paragraph 3 of that order reads, and I quote, "This temporary order shall become effective immediately upon service on MCorp and shall remain in full force and effect pending the completion or termination of the administrative proceedings initiated pursuant to the foregoing amended notice, except" -- and so forth.

Now, the position of the Board on that issue, Chief Justice, has been that that order was suspended. And indeed, that order was temporarily suspended by a letter that is at pages 184 and 185 of the joint appendix, dated November 7, 1988. But 6 months later, the Board, on the 24th of May, and during the pendency of the Chapter 11 case, and this is at page 194 of the joint appendix, wrote in a notice of charges, "The provisions of this second amended notice do not supersede, modify, or in any manner affect the provisions of the notice of charges and of hearings issued against MCorp and MCorp management, Dallas, Texas, by the Board of Governors on March 30" -- and the important part -- "or the status of the temporary orders issued on October 19 and 26, 1988."

QUESTION: Now did the court of appeals view these orders that you've just quoted the same way you did or you do?

MR. MILLER: I don't believe the court of

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

appeals considered them.

QUESTION: Well, you know, we grant certiorari on certain cases, and as Justice White says, we're not interested in having what we think is a case turn into a noncase, that just goes off on facts that either we weren't aware of or the court of appeals below didn't consider.

MR. MILLER: But the court of appeals was considered below an important issue. And that was whether the statutory foundation for the issuance of this order, that is to say the alleged source-of-strength doctrine, exists and is valid or whether no such statutory basis exist.

QUESTION: Well, I had thought, please correct me if I'm wrong, that in any entity subject to one of these orders has the right to appeal to the circuit court and that only the circuit court's order makes it enforceable. Please correct me if that's wrong.

MR. MILLER: I believe it's almost right, Justice Kennedy. In fact, temporary orders may be revoked, suspended, or modified by a district court. I believe the right provision is 1818(c)(2). It is final orders that go to the court of appeals.

Here, immediately after the temporary order that I read from, and one other -- indeed two others were

issued -- MCorp before the bankruptcy went to the District Court for Northern District of Texas under Section 1818(c)(2) and sought immediately to have that order revoked, suspended, or modified. The letter that I read to the Court represented an agreement by the Board of Governors to temporarily suspend the temporary order, and that continued until the bankruptcy was filed. It was after the bankruptcy that the Board, as I read from the notice of charges in May, then said, that's really reinstated.

So we have --

QUESTION: But I still take it that the entity MCorp is under no obligation to make an actual transfer of proceeds until the circuit court affirms the order of the Federal Reserve Board.

MR. MILLER: Not at all. It believe they were as soon as the suspension -- the bankruptcy was filed and the suspension was effectively lifted by the Board. The order that I read you said that it will make all available assets will be transferred to the banks. And that's where the tension arises.

And what the Board is attempting --

QUESTION: Well, I want to make it very clear, is MCorp entitled to have a stay of that order pending its consideration by the court of appeals?

MR. MILLER: We believe it was.

QUESTION: All right, then I don't see how you come and you say, oh, all these assets are being transferred out of MCorp. That just isn't happening because the court of appeal's review stays it.

MR. MILLER: The Board -- the Board took the position that the temporary order requiring the down-streaming of the assets was in full force and effect. MCorp went into the district court in the Chapter 11 case -- actually went into the bankruptcy court; the Board moved the case up to the district court -- and went into the district court and said this order has no legitimate statutory foundation. These temporary orders ought to be stayed immediately. And furthermore, there's no purpose in going forward with a permanent proceeding because there is no validity to the source of strength.

So we do have a very live controversy in the bankruptcy and in the Northern District of Texas on these issues. It is the 1334(b) jurisdiction under Title XXVIII that gave the bankruptcy court as well concurrent jurisdiction with the Northern District to review the temporary orders.

QUESTION: Well, suppose we think that the bankruptcy law that speaks of what court shall have exclusive or concurrent jurisdiction doesn't apply to

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

ongoing administrative proceedings in an agency such as this board, and so that we think that section simply is inapplicable. Now suppose that's the situation, then where are you with regard to enforcement of the temporary order that says go ahead and pay all your assets over.

MR. MILLER: Then, Justice, it seems to me that we must examine whether or not this order to put all the assets from the holding company into the banks has any -- valid statutory source. Otherwise, there is never an opportunity to review that before the entire holding company assets are eviscerated, the Chapter 11 is over, and the banks effectively have collapsed with the 400 or whatever million dollars have been placed in them. It cannot be that the Court has no power to examine whether or not the underlying basis for the Government's assertion of the source of strength has any sound statutory footing.

Indeed, there is as well as it relates to the temporary orders, the automatic stay. I only referred to one of the temporary orders that are at issue here. There is a second temporary issue ordered 1 week earlier. And that also was never suspended by the board pursuant to the letter agreement, never suspended by any agreement. That order required that MCorp not dissipate any of its assets. Dissipation is a term used by the Board included, unless otherwise accepted, paying your debts. And indeed that

temporary order which is also in the record, said that MCorp could continue to pay debts previously contracted and it could continue to pay salaries -- these were exceptions to dissipation -- but it couldn't contract for any new goods or any new services, barring consent of the Federal Reserve Bank in Dallas.

And that order was in full force and effect when the bankruptcy was filed. The automatic stay of the Bankruptcy Code prohibits anyone from taking any act to control the assets of a debtor or to obtain possession. Now that is not the section that Mr. Minear referred to. That is Section 362(a)(3).

QUESTION: Well, the automatic stay, though, I assume, presupposes that the bankruptcy court has some jurisdiction.

MR. MILLER: Yes, it does, Justice.

QUESTION: And maybe it doesn't here of a case where there's no final administrative order.

MR. MILLER: But the automatic stay is a congressional edict. It doesn't require an act of a court to exercise or put in place the automatic stay.

QUESTION: Yeah, but I think it presupposes a bankruptcy court with jurisdiction. And perhaps that isn't what we have here.

MR. MILLER: But Congress also gave, under

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

1334(d), exclusive jurisdiction of the assets of a debtor wherever located to the bankruptcy court. And obviously, since the 1334(d) was enacted in 1984, it well succeeded the enactment of 1818(i).

QUESTION: When you went into the bankruptcy court, Mr. Miller, when you sought a stay in the district court, did you rely on the automatic stay provisions?

MR. MILLER: Yes, we did. I believe that the record will reflect we asked for two things. We asked for a declaratory judgment that the automatic stay applied, and we asked for a Section 105 stay, which is the bankruptcy equivalent of the All Ritz Act against prosecution. We did so because the automatic stay applies with regard to the -- any act to control assets of the estate are to obtain possession of the estate, and there are no exemptions to that in Section 362(b), none whatsoever.

But in addition to that, the legislative history to Section 362(a) indicates quite clearly that the exemptions relied upon by the Board, and maybe overturned by the bankruptcy court in its discretion under the authority granted under Section 105(a). It shifts the burden to the debtor or other trustee to seek that stay, but it does not by virtue of section 362(b) disable a Chapter 11 debtor or a trustee from obtaining a stay under

Section 105.

QUESTION: Now let me just understand. So you're now -- you're saying that as of now, debts are being paid and properties are being transferred quite beyond the control or authority of the bankruptcy court to stay.

MR. MILLER: No, I'm not saying that at all. What I'm saying is that, during the Chapter 11, administrative expenses may be paid despite the temporary order of the Board of Governors which would say that without their consent you cannot pay salaries, you cannot pay your lawyers to come to the United States Supreme Court, you cannot pay anything without the control of the Federal Reserve Bank in Dallas being exercised.

What we're saying is, yes, the exclusive jurisdiction of Title XXVIII authorizes the court to administer the Chapter 11 case and to administer the assets during the Chapter 11 free from interference with the control over those assets by the Board of Governors.

I hope I've answered your question, Justice.

QUESTION: I gather you're also telling us the Board hasn't tried to enforce that order, that letter.

MR. MILLER: It couldn't because, first --

QUESTION: It never did try to. So that really isn't an issue before us, is it?

MR. MILLER: Oh, it is. It is because we cannot -- if the Board were to have its way, we could not propose a plan of reorganization that would create new indebtedness because that temporary order would be staring us in the face.

QUESTION: You also couldn't pay your lawyers.

MR. MILLER: That's is correct.

QUESTION: But you are paying your lawyers.

MR. MILLER: Because there is a stay outstanding from the court of appeals that permits us to carry on the business of these debtors. But for that stay, or for the graciousness, if you will, of the Board of Governors, we would be unable to pay those obligations, Justice Stevens.

QUESTION: And is the validity of that stay what we're reviewing now?

MR. MILLER: Yes. Because the validity of that stay is based on the source of strength. The source of strength is the basis for the issuance of the temporary orders.

QUESTION: Oh, okay.

MR. MILLER: Indeed, the temporary orders were first initiated as a procedure preliminary to the final findings on the source-of-strength doctrine initiated by the Board of Governors in the fall of 1988.

Now, we need not, we think, rely merely on the

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

Leedom analysis of the court of appeals. We think the analysis is sound, but more importantly we think that statutory framework in which the source-of-strength charges were brought, and its counterpoint with the bankruptcy require an examination by the bankruptcy court of whether or not the proceeding may go forward. And the reason for that is that there is an automatic stay under Section(a)(1), and here we're now -- we're off the issue of the temporary orders, and we're on to the main proceedings. And (a)(1) prohibits any suit or proceeding, including an administrative proceeding, that could have been brought prior to a filing of a petition from going forward.

Now, the Board relies upon the exemption in Section 364 -- Section 362(b)(4), which says that a governmental unit proceeding under Section(a)(1) to enforce its police or regulatory power may, nevertheless, despite Section(a)(1), go forward to the point of judgment unless the judgment is a nonmonetary judgment. And then under Section (b)(5) for injunctive relief, it may be enforced.

The issue then arises, it seems to us, for the bankruptcy, or here, the Article III district court, to determine whether this is a legitimate police or regulatory power enforcement action. Is there a police

power or a regulatory power to be enforced? Because if there is not, then seemingly subsection(a)(1), the automatic stay, would apply, and at that point the proceeding would be automatically stayed.

QUESTION: Well, that would mean you would have some sort of a merits inquiry with respect to every regulatory investigation that was being undertaken by the Government. You would say this exception doesn't apply unless there is authority for the Government agency to conduct this sort of regulation.

MR. MILLER: We believe that in a bankruptcy, where the nature of the proceeding is one that is calculated to lead to the removal of the assets of a holding company, yes, that under those circumstances, the Court necessarily must examine whether there is a police or regulatory power, Chief Justice.

QUESTION: You say calculated to lead, Mr. Miller, but reading the court of appeals opinion here, (2)(a) and (3)(a) of the petition for certiorari, it seems to me the court of appeals did not feel it was presented with your temporary stays that might have had the effect of removing -- it's talking about notice of charges and hearings that were to be conducted. They didn't think there was any prospect of property being removed unless an order became final.

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

MR. MILLER: Correct.

QUESTION: So what you're calling our attention to in these temporary orders was never called to the attention of the court of appeals. Is that correct?

MR. MILLER: No, it was called to the attention of the court of appeals.

QUESTION: Well, they didn't consider them in their opinion.

MR. MILLER: They didn't refer to it. And I was not just now referring to the temporary orders. I was referring to the notice of charges that Your Honor --

QUESTION: And that's why you had calculated to because certainly unless -- until the administrative proceeding becomes final and is subject to some sort of review, it isn't going to have the effect of removing any property.

MR. MILLER: That is correct. Without the temporary orders, obviously. But here, we have a Chapter 11 case effectively being held hostage to the long process of the administrative proceeding to determine the propriety of the source of strength. We're not just in the administrative proceeding going to get into is there a statutory basis. We're now going to get into, during these proceedings, what are the needs of the banks, what are the capital of the banks, how much is it going to be

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

going forward and backwards. It's going to be a long and difficult proceeding.

And as this Court, we believe, urged in Timbers, the job in the Chapter 11 is to get on with it, not to prejudice the creditors who are creditors of the holding company, be they secured or unsecured, by a long proceeding, but to get on with it. And if the court, an Article III court, were to determine that there is no legitimate source-of-strength power, then it would seem to us that the court, in determining whether the automatic stay is in effect or not, has the ability to determine that issue. In effect, it's really determining if it has jurisdiction because under Section 1818(i), which is the preclusion or deferral statute, even the section says that no court shall take action by injunction or otherwise to stay a notice or an order issued under this section.

So the question is, is the order really issued under this section. Is there a statutory power to enforce the source of strength.

Now on that issue, we would submit that the record is hopelessly deficient to demonstrate a source-of-strength power. The only statute that comes close to authorizing a review of financial or managerial prospects and resources of the holding company is 1842(c), and that is that is the same statute that was reviewed by this

Court in First Lincolnwood.

QUESTION: Doesn't this get you back into a sort of Leedom kind of analysis? I mean --

MR. MILLER: I'm reluctant to call it a Leedom kind of -- it is a Leedom type of analysis.

QUESTION: Type of analysis. You're saying that there's no proceeding under this section if the proceeding is not proper under the section.

MR. MILLER: Correct.

QUESTION: Do you think that's what the statute means?

MR. MILLER: Well, I think that 1818(i), which requires that you proceed either in the district court on temporary orders or in the court of appeals on final orders, is analogous to an exhaustion statute. And I think there are two attacks to an exhaustion statute: one, a constitutional collateral attack, and the other, the question of whether the agency is proceeding in fulfillment of a valid statutory purpose.

And it is that analysis that we're asking the Court to make here on the source of strength. Because the only statute that relates to this is 1842(c), and that in a very limited sense authorizes the Board of Governors to look at the financial and managerial prospects at the time of acquisition or merger, not to give it a continual let's

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

look at the financial resources and prospects and let's allow the Board of Governors to make an unlimited capital assessment of a holding company's assets for all time's sake. That would be an extraordinary transfer of the wealth of the holding company to the banks for the benefit of the FDIC. And there is nothing in this statute that seems to indicate the power on the part of the Board of Governors.

Nor is there, we submit, in any other legislation, such a power. Indeed, in the thirties, in the 1930's, the Congress of the United States eliminated the shareholder assessment capability in a serious of four amendments in 1933, I believe 5, and then later stretching into the 1950's, despite testimony during those hearings, which is cited in our brief, that by the Comptroller of the Currency, that this was a valuable tool in allowing the regulatory authorities to work with the stockholders and management of then-troubled and failing banks.

So that the Congress made a fundamental policy decision in the thirties to eliminate capital assessment abilities. And it is in the face of that elimination that the Board, nevertheless, seeks to enforce the source-of-strength doctrine here, under the guise of this very vague statutory term of unsafe and unsound, which we think could be interpreted to mean anything.

This relief is extraordinary to say to an independent corporation, formed with its own shareholders and its own creditors, you must transfer all of your assets into your banks, whether or not it's going to help you. You must denude yourself of all of your assets. That just can't be the law without an express direction from the Congress, we submit.

QUESTION: Well, at the conclusion of these administrative proceedings to which you object, if there was a final cease-and-desist order, would that be subject to judicial review?

MR. MILLER: The final would be subject to review in the court of appeals.

QUESTION: And would the validity of the regulation be at issue? Could it be an issue?

MR. MILLER: Yes, it could be an issue, Justice White.

QUESTION: So it's just a question of when you get this adjudication.

MR. MILLER: Well, the difficulty with that is that the standard for review in the court of appeals, it would seem to me -- as best I recollect it would be -- whether or not the agency action is arbitrary and capricious. That is -- I'm not sure that necessarily that would involve -- I guess it would involve the

determination of whether there was power.

QUESTION: I don't think that's a standard for deciding whether the regulation is consistent with the statute.

MR. MILLER: Well, it would be a question of deciding --

QUESTION: A question of statutory construction or --

MR. MILLER: -- whether the determination was appropriate, and I think under those circumstances, the Administrative Procedures Act requires a finding.

QUESTION: And why is it, in a word, your opportunity for judicial review at the end of this proceeding wouldn't be adequate for your purposes?

MR. MILLER: If we're just referring to the notice of charges, it seems to me that what we've done then is hold hostage the Chapter 11 that Congress has authorized the bank holding company to take advantage of until the long road at the end of the administrative proceeding. And that since this is a purely legal issue, it is not factual driven at all, this could be considered well before that by a court in the context --

QUESTION: Well, I suppose you make this argument whether any of the assets of the bank holding company are in danger now.

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

MR. MILLER: That is correct.

QUESTION: It's just the fact -- just the fact that you -- that the bankruptcy proceeding is being interfered with while the administrative proceeding going on?

MR. MILLER: It's the determination of the extent to which the administrative proceeding is automatically stayed by the congressional act of Section 362(a). It is in that context that I make that suggestion, Justice.

QUESTION: I think the delay is really the only problem, Mr. Miller, isn't it? I mean, the standard of review is going to be exactly the same. It isn't just arbitrary and capricious. It says arbitrary, capricious, and abuse of discretion or otherwise not in accordance with law. I mean, if it is a violation of law, it's a violation of law.

MR. MILLER: I think that's correct. Yes, Justice. That is correct.

To the point on the merits of source of strength, we would also point to the many, indeed I suspect a dozen, legislative initiatives that have occurred since 1987 when the Board of Governors first announced -- announced for the first time in some 30 years -- what the source of strength, at least in its view, was

all about. It first indicated that the regulation why, under which it was purporting to adopt a policy statement, had something to do with down-streaming of assets from holding companies to banks. And subsequent to that date, virtually every other regulator has taken the position that this is either flawed, it doesn't exist, or it shouldn't exist for a variety of policy reasons.

Accordingly, it is our belief that the Court should defer to the Congress on the question of source of strength, require the Congress, if you will, if they determine that it's appropriate to have a source of strength, to so state. And as a consequence, we would ask that the Court affirm the court below.

That concludes my remarks. And, of course, I would be happy to answer questions of the Court.

QUESTION: Counsel, one question. During the pendency of these proceedings, has MCorp divested itself of any of the banks in question?

MR. MILLER: Yes. If I could just take 1 minute. Before the proceeding began -- that's not quite accurate. An involuntary proceeding was filed on March 20 -- I think it's March 24 of 1989. About 4 or 5 days later, 20 of the 25 banks were closed by the Comptroller of the Currency.

QUESTION: What about the remaining five?

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

MR. MILLER: Of the remaining five, four have been sold during the Chapter 11 proceeding, one remains.

QUESTION: Which one is that?

MR. MILLER: The name of the bank is Ambank New Braunfels, N-e-w B-r-a-u-n-f-e-l-s.

QUESTION: And that keeps the proceeding live in the Federal Reserve Board as to that bank?

MR. MILLER: I'm not sure what the position of the Federal Reserve Board is on whether this proceeding would be obviated by a disposition of that bank.

QUESTION: Thank you, Mr. Miller.

Mr. Minear, do you have rebuttal?

REBUTTAL ARGUMENT OF JEFFREY P. MINEAR

ON BEHALF OF THE FEDERAL RESERVE SYSTEM

MR. MINEAR: Yes, Your Honor, I do.

I'd like to begin with this question of the temporary cease-and-desist order, since it's been raised again. This is something that we addressed in a supplemental brief in response to MCorp's supplemental brief. As an initial matter, these three temporary cease-and-desist orders are all the subject of a pending judicial action in the Northern District of Texas. The complaint is set forth at page 174 of the joint appendix. So if you lift the injunction in this case, then it will then turn to that judicial action in turn of the status of

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

the temporary orders.

It's our belief that the continued viability of these order 3 years later is open to question. In the earlier proceeding, MCorp itself had raised that point. At 116 of the joint appendix, they make the argument that these temporary orders are in fact moot. They might well be. And that is something that could be determined in the Northern District of Texas in the judicial proceeding that they had filed, a separate judicial proceeding.

Additionally, I'd like to touch upon this question of the title of the Board's action of eviscerating the bankruptcy --

QUESTION: Excuse me, Mr. Minear, before you go on, you acknowledge those orders are outstanding or you do not?

MR. MINEAR: Two of the orders are outstanding, but we think that they are in effect, or their effect is questionable because of the bankruptcy proceeding. There is a judicial action to challenge them, but nothing has gone forward because the stay that's in effect in this case has prevented anything from going forward. The Board might take some action to withdraw those temporary orders, but it can't do anything until we resolve this proceeding first.

With respect -- those two are -- to get into the

details of this, one order provided that MCorp would not pay any dividends. The bankruptcy court has stayed that, the payment of dividends, as well.

The second order prohibited any extraordinary disbursements or expenditures, such as bonuses to management. We believe the bankruptcy court will prevent that from taking place as well, so the orders, in effect, have no practical effect at this point.

The third order concerned the source-of-strength proceeding. And as we explain in our supplemental brief, the Board has suspended the operation of that temporary order. And the language that Mr. Miller quotes concerning the second amended notice of charges that preserves the status of the temporary orders, it preserves the status of that order as being suspended.

So in effect, these temporary orders are just not a part of the case. That's simply a red herring that I think that MCorp has raised.

With respect to the bankruptcy proceeding being eviscerated by the Board's challenges, I think it's important to note that in our second amended notice of charges, the amount of capitalization that we indicated we felt would be necessary with respect to four of the five remaining banks was $21 million. MCorp has asserted in the bankruptcy proceeding that it has assets of 1.5

billion. So I think that there's -- you know, a difficulty with that, the argument that they make here on that point.

Concerning the long process that would be involved here, according to the stipulation of our proffer of facts that MCorp offered, the hearing before the Board would take 3 days on the part of the Board and 3 days on the part of MCorp. If this proceeding had gone forward as planned, it would have been completed long before this. Reorganization would be completed.

As far as the record deficiencies, I think that that is quite true that there are deficiencies in the record. And the very reason there are deficiencies in the record here is because of the injunction that has prohibited any evidentiary hearing to flush out a lot of the allegations that Mr. Miller is making at this point.

Finally, with respect to the question of extraordinary relief here, I think that the question of relief is something that we'll just have to wait for the ongoing proceeding to determine. The important point is to remember again, Section 1818(i), which provides that no court may take any action to enjoin the Board's proceedings except in accordance with that section. That is the matter that's at issue here.

Unless there are any further questions, thank

you, Your Honor.

CHIEF JUSTICE REHNQUIST: Thank you, Mr. Minear.

The case is submitted.

(Whereupon, at 12:01 p.m., the case in the above-entitled matter was submitted.)

ALDERSON REPORTING COMPANY, INC.
1111 FOURTEENTH STREET, N.W.
SUITE 400
WASHINGTON, D.C. 20005
(202)289-2260
(800) FOR DEPO

CERTIFICATION

Alderson Reporting Company, Inc., hereby certifies that the attached pages represents an accurate transcription of electronic sound recording of the oral argument before the Supreme Court of

The United States in the Matter of: 90-913 , 90914
BOARD OF GOVERNORS FEDERAL RESERVE SYSTEM OF THE UNITED STATE
Petitioner, v. MCORP FINANCIAL, INC., ET AL. and

MCORP, ET AL., Petitioners, v. BOARD OF GOVERNORS OF THE FED
RESERVE SYSTEM OF THE UNITED STATES.

---

and that these attached pages constitutes the original transcript of the proceedings for the records of the court.

BY _____

(REPORTER)