

4. Assets Acquired in Assistance to an Insured Bank:

On July 26, 1984, the FDIC, the Federal Reserve Board, the Comptroller of the Currency and a group of major U.S. banks agreed to provide a "permanent assistance program" to the Continental Illinois National Bank and Trust Company of Chicago ("CINB") and its parent, Continental Illinois Corporation. This program, which became effective on September 26, 1984, after Continental Illinois Corporation shareholder approval, replaced a temporary, emergency assistance package among the same parties that had been in effect since May 1984. Major elements of the new package included a financial assistance plan to remove problem loans from CINB and infuse new capital resources into CINB, the continuation of on-going lines of credit from the Federal Reserve Board and a group of major U.S. banks to alleviate liquidity pressures and the installation of a new management team. Additionally, the FDIC agreed to commit more capital or other forms of assistance if the permanent assistance program proves to be insufficient for any reason.

The key aspects of the permanent assistance program applicable to the FDIC are embodied in an Implementation Agreement and an Assistance Agreement between the FDIC and CINB, Continental Illinois Corporation, and Continental Illinois Holding Corporation, a new holding company formed to own all Continental Illinois Corporation stock as of the effective date for the purpose of implementing the FDIC Option (described below). Discussed below are the major aspects of the FDIC's participation in the permanent assistance program and their effect on the FDIC financial statements.

The assets acquired by the FDIC in assistance to CINB on the commencement date and as of year end are as follows (in thousands):

	(Commencement Date) September 26, 1984	December 31, 1984
Loans and related assets purchased	\$2,000,000	\$2,010,313
Promissory note	1,500,000	1,447,116
Preferred stock investment	<u>1,000,000</u>	<u>1,000,000</u>
	\$4,500,000	\$4,457,429

Loans acquired were selected by CINB with the restrictions that such loans were nonperforming, classified or otherwise of poor quality (i.e., "troubled loans"). Certain foreign loans were excluded from selection. On September 26, 1984, after consummation of the permanent assistance program, CINB transferred \$2.0 billion of troubled loans to the FDIC. The unpaid legal principal value of these loans was approximately \$3.7 billion.

Also, on September 26, 1984, the FDIC received a promissory note from CINB for \$1.5 billion. At CINB's option, the promissory note can be paid anytime within three years by transfer of additional troubled loans (subject to the above restrictions) at CINB's book value as of the date of transfer. Until such time as the promissory note is paid, interest will be charged. As of December 31, 1984, CINB transferred \$52,844,000 of additional troubled loans to the FDIC as partial repayment on the original promissory note. As a result, the remaining unpaid principal balance on the note is \$1,447,116,000.

The purchase of these assets was, in part, funded by the assumption of \$3.5 billion of indebtedness to the Federal Reserve Bank of Chicago (FRB) on behalf of CINB. These borrowings will bear interest at specified rates established by the FRB and the U.S. Treasury. The FDIC will repay these borrowings by making quarterly remittances of its collections, less expenses, on the troubled loans. If there is a shortfall at September 26, 1989, the FDIC will make up such deficiency with its own funds.

Assets Acquired in Assistance to an Insured Bank (continued):

The Implementation Agreement provides for the FDIC to be reimbursed each quarter for its expenses related to administering the transferred loan portfolio and for interest paid on the indebtedness to the FRB which it assumed. Thus, such costs are recorded as assets. The FDIC and CINB have entered into a service agreement whereby CINB will administer the transferred loan portfolio on behalf of the FDIC. The FDIC is also permitted to establish a special reserve account from troubled loan collections. The balance in this account, if any, reverts to the FDIC in those quarters when loan collections have been insufficient to cover interest owing on the indebtedness which it assumed. For financial accounting purposes, cash collections received on the transferred loan portfolio (plus certain other amounts) are applied quarterly in accordance with the Implementation Agreement terms, as follows: 1) to the administrative expenses paid by the FDIC; 2) to the interest owing on the assumed indebtedness; 3) to fund the special reserve account such that this account plus accrued interest thereon is at least \$75 million; and 4) to principal owing under the FRB Agreement. The FDIC is entitled to receive interest on the cumulative deficiencies between cash collections and the costs incurred in administering the troubled loans and the interest on the assumed debt. Further, CINB has assigned to the FDIC all its existing and future claims against any party which may be related to any loss incurred in connection with any transferred loan.

Total cash flow consists of the above collections of principal and interest on the transferred loan portfolio, interest payments on the CINB promissory note and interest earned on daily collections. As of December 31, 1984, the FDIC received cash flow totaling \$147,044,000. Cash flow was applied to administrative costs and interest expense of \$3,224,000 and \$94,564,000 respectively, and to establish a special reserve account balance of \$49,256,000. Accordingly, total FDIC obligations for purposes of exercising the FDIC option (discussed below) are \$3.457 billion. The collection results during this period should not necessarily be considered indicative of the ultimate loan portfolio collectibility.

Ultimate collection results on the transferred loan portfolio are subject to significant uncertainties because of the financially troubled nature of the borrowers and the effects of general economic conditions on their industries. Due to the number and complexity of the loans within the transferred loan portfolio, an estimate of the ultimate collectibility has not been completed by the FDIC. Accordingly, no determination has been made as to whether or not any allowance for loss related to the CINB permanent assistance program is necessary. Consequently, none has been recorded in the financial statements for the year ended December 31, 1984. The Corporation expects to complete its initial determination of the estimated net realization on the transferred loan portfolio during 1985.

The FDIC holds an option to acquire up to 40.3 million shares of Continental Illinois Corporation common stock. The shares subject to the option are owned by Continental Illinois Holding Corporation, which is owned by the former stockholders of Continental Illinois Corporation. The option cannot be exercised prior to the fifth anniversary of the commencement date, September 26, 1989. Further, the option is exercisable only if the FDIC suffers a loss (disregarding any profit or loss from the FDIC's interest in Continental Illinois Corporation preferred or common stock) on the transferred loan portfolio, including unrecovered administrative costs and interest expense. If the FDIC suffers a loss, the FDIC will be entitled to retain any remaining transferred loans and to exercise the FDIC Option for one share of Continental Illinois Corporation common stock for every \$20 of loss, at the exercise price of \$0.00001 per share of common stock. No value has been assigned to the FDIC's right to exercise this option as of December 31, 1984. If the FDIC does not suffer any loss under the permanent assistance program, all remaining loans and other assets acquired will be returned to CINB and the option would not be exercisable.

The FDIC also purchased \$1 billion of two non-voting, Continental Illinois Corporation, preferred stock issues. The proceeds of these issues were transferred to CINB in the form of a capital contribution. The Junior Perpetual Convertible Preference Stock, in the amount of \$720 million, is convertible into 160 million shares of Continental Illinois Corporation common stock upon sale or transfer by the FDIC. Dividends are to be received on this preferred stock only to the extent that dividends are paid on the Continental Illinois Corporation common stock and are equivalent to that which would be paid on 160 million shares of common stock. The Adjustable Rate Preferred Stock, Class A, in the amount of \$280 million, is a cumulative issue that is callable at the option of Continental Illinois Corporation. The issuer also has the option to pay dividends on this issue in the form of additional shares of this issue or cash until the third anniversary of their original issue date.