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FEDERAL DEPOSIT INSURANCE CORPORATION

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12 CFR Part 380

Enforcement of Subsidiary and Affiliate Contracts by the FDIC as Receiver of a Covered Financial Company

RIN 3064-AD94

AGENCY: Federal Deposit Insurance Corporation.

ACTION: Final rule.

SUMMARY: The Federal Deposit Insurance Corporation (the "FDIC" or the "Corporation") is issuing a final rule ("Final Rule") that implements section 210(c)(16) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act" or the "Act"), codified at 12 U.S.C. section 5390(c)(16), which permits the Corporation, as receiver for a financial company whose failure would pose a significant risk to the financial stability of the United States (a "covered financial company"), to enforce contracts of subsidiaries or affiliates of the covered financial company despite contract clauses that purport to terminate, accelerate or provide for other remedies based on the insolvency, financial condition or receivership of the covered financial company. As a condition to maintaining these subsidiary or affiliate contracts in full force and effect, the Corporation as receiver must either: (1) transfer any supporting obligations of the covered financial company that back the obligations of the subsidiary or affiliate under the contract (along with all assets and liabilities that relate to those supporting obligations) to a bridge financial company or qualified third-party transferee by the

statutory one-business-day deadline; or (ii) provide adequate protection to such contract counterparties. The Final Rule sets forth the scope and effect of the authority granted under section 210(c)(16), clarifies the conditions and requirements applicable to the receiver, addresses requirements for notice to certain affected counterparties and defines key terms.

EFFECTIVE DATE: [Insert date 30 days after publication in Federal Register].

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SUPPLEMENTARY INFORMATION:

Title II of the Dodd-Frank Act provides for the appointment of the FDIC as receiver of a covered financial company that poses a systemic risk to the nation's economic stability and outlines the process for the orderly resolution of a covered financial company following the FDIC's appointment as receiver. Section 209, codified at 12 U.S.C. section 5389, authorizes the FDIC, in consultation with the Financial Stability Oversight Council ("FSOC"), to prescribe rules and regulations as the FDIC considers necessary or appropriate with respect to the rights, interests and priorities of creditors, counterparties, security entitlement holders or other persons with respect to any covered financial company and other matters necessary or appropriate to the implementation of the orderly liquidation authority established under Title II of the Act. Pursuant to the authority granted by section 209, the FDIC is issuing the Final Rule.

I. Background

Fundamental to the orderly liquidation of a covered financial company is the ability to continue key operations, transactions and services that will maximize the value of the firm's assets and operations and avoid a disorderly collapse in the marketplace. To facilitate this continuity of operations, the Dodd-Frank Act provides several tools to preserve the value of the covered financial company's assets and business lines, including the powers granted in section 210(c)(16), codified at 12 U.S.C. 5390(c)(16) ("section 210(c)(16)" or the "Statute"). Specifically, section 210(c)(16) provides that the Corporation, as receiver for a covered financial company, has the power "to enforce contracts of subsidiaries or affiliates of the covered financial company, the obligations under which are guaranteed or otherwise supported by or linked to the covered financial company, notwithstanding any contractual right to cause the termination, liquidation, or acceleration of such contracts based solely on the insolvency, financial condition, or receivership of the covered financial company, if (i) such guaranty or other support and all related assets and liabilities are transferred to and assumed by a bridge financial company or a third party . . . or (ii) the Corporation, as receiver, otherwise provides adequate protection with respect to such obligations."

The conditions contained in (i) and (ii) of the quoted statute assure counterparties that any contractual right to guaranties or other support, including claims on collateral or other related assets, would be protected. Thus, section 210(c)(16) requires, as a condition to the authority to enforce subsidiary or affiliate contracts that are "linked to" the financial condition of the covered financial company through a default provision, that the Corporation as receiver transfer any guaranty or other support provided by the specified

covered financial company for the contractual obligations together with all related collateral to a bridge financial company or other qualified transferee within one business day after its appointment as receiver. In the alternative, if the receiver does not transfer the support and the related assets and liabilities, the receiver must provide "adequate protection" with respect to any support or collateral not transferred in order to preserve its right to enforce the contract of the subsidiary or affiliate.

In providing the orderly liquidation authority of Title II, the Dodd-Frank Act provides certain particular authorities with respect to subsidiaries and affiliates of the covered financial company. For instance, section 210(a)(1)(E) of the Dodd-Frank Act provides an expedited procedure to allow the Corporation to appoint itself as the receiver of certain subsidiaries of a covered financial company if the Corporation and the Secretary of the Treasury jointly determine that such subsidiary is in default or in danger of default and that such action would mitigate serious adverse effects on the financial stability of the United States and would facilitate the orderly liquidation of the covered financial company. That section further provides that upon such an appointment, the subsidiary would be treated as a covered financial company and the Corporation would be able to exercise the full range of special powers available to the receiver.

In certain cases, however, the receiver for the covered financial company may find that the best course of action to maximize the value of the covered financial company and to mitigate systemic risk would be to avoid actions that place subsidiaries in danger of default or that necessitate complex interlocking receiverships. The affiliated legal entities that collectively comprise a complex financial institution typically share and provide intra-group funding, guaranties, administrative support, human resources and

other operational and business functions. Some of these operations and activities may be critical to the day-to-day functions and overall operations of the group. In addition, certain significant subsidiaries of a covered financial company may be essential to core business lines or may conduct critical operations that, if discontinued, may threaten the stability of the financial markets. In these circumstances, orderly liquidation of a covered financial company may best be accomplished by establishing a single receivership of the parent holding company and transferring valuable operations and assets to a solvent bridge financial company, including the stock or other equity interests of some or all of the company's various subsidiaries. Accordingly, the Dodd-Frank Act provides the FDIC with the tools and flexibility to act effectively as receiver for the covered financial company at the holding company or parent level without placing solvent subsidiaries into receivership. This approach may be the best means of preserving value, minimizing the shock to the financial system, providing additional flexibility to mitigate cross-border resolution issues for global systemically-important financial companies and allowing for a more expeditious resolution of a covered financial company.

Where such an approach is adopted, the powers granted to the receiver under section 210(c)(16) are essential to preservation of going-concern value of the subsidiaries for the benefit of the parent in receivership. Absent this statutory provision, counterparties to contracts of subsidiaries and affiliates could exercise contractual rights to terminate their agreements based upon the insolvency of the specified covered financial company. As a result, otherwise viable affiliates of the covered financial company could become insolvent, thereby inciting the collapse of interrelated companies and potentially amplifying ripple effects throughout the economy.

As described in more detail below, the Final Rule clarifies the scope of the authority granted in section 210(c)(16) as well as conditions and requirements applicable to the receiver. The Final Rule makes clear that the effect of this enforcement authority is that no party may exercise any remedy under a contract simply as a result of the appointment of the receiver and the exercise of its orderly liquidation authorities as long as the receiver complies with the statutory requirements. The Final Rule addresses requirements for notice to affected counterparties and defines key terms. It also clarifies the term "adequate protection" in a manner consistent with its interpretation under the Bankruptcy Code.

On March 27, 2012, the FDIC published a notice of proposed rulemaking ("NPR") relating to the enforcement of subsidiary and affiliate contracts by the Corporation as receiver of a covered financial company under section 210(c)(16) (77 FR 18127, March 27, 2012). The NPR, which included proposed rules (the "Proposed Rule"), requested comments on all aspects of the Proposed Rule and included specific questions as to several aspects of the Proposed Rule. The comment period ended on May 29, 2012. The FDIC considered all of the comments received in response to the NPR.

In accordance with section 209 of the Act, the FDIC reviewed otherwise applicable insolvency law, including the Bankruptcy Code, and has harmonized the Final Rule with such laws where possible. Such harmonization includes the formulation of the definition of adequate protection, which is generally consistent with Bankruptcy Code precedent. Also consistent with Section 209 of the Act, the FDIC consulted with the FSOC in preparing the Final Rule.

II. Summary of Comments on the Proposed Rule

The FDIC received six comments in response to the Proposed Rule. Two letters were from individuals and fully supported the Proposed Rule. The other four letters, of which two were submitted by insurance industry trade groups, one by an insurance underwriter and one jointly on behalf of three financial industry associations, proposed that various changes should be made to the Proposed Rule. The FDIC also held a follow-up teleconference at the request of one of the authors of the financial industry association letter.

One of the areas of concern to commenters related to how the rule would be applied. The letter from the financial industry associations expressed concern that by defining "specified financial condition clause" to include provisions permitting a counterparty to exercise remedies based directly or indirectly upon a change in the financial condition or the insolvency of the covered financial company, the Proposed Rule could be construed to prohibit the exercise of remedies by reason of an actual default by a subsidiary or affiliate of the covered financial company. One example cited in the letter was a payment default by a subsidiary which relied on its parent for funds with which to make contractual payments to its counterparties. The letter stated that if the subsidiary were to default on a payment obligation because the parent covered financial company was no longer capable of providing it with necessary funds, it could be argued that the default arose as a result of a change in the financial condition or the insolvency of the covered financial company.

This outcome is not intended by the Proposed Rule, and language has been added to the preamble to further clarify this point. Although the Final Rule prohibits the exercise of remedies based upon specified types of actions or circumstances relating to a covered financial company or one of its direct or indirect transferees, the Final Rule does not prohibit a termination or exercise of other remedies based upon a default under a contractual provision that relates solely to a breach or default by the subsidiary or affiliate. Thus, the rule would not affect a counterparty's rights if the subsidiary or affiliate fails to make a payment due a counterparty. Of course, if the subsidiary or affiliate were to be in default under its contract because the subsidiary or affiliate did not comply with a proscribed remedy for an asserted violation of an unenforceable specified financial condition clause, the Final Rule does not permit the counterparty to take action on the basis of that default. Thus, for example, if a contract of a subsidiary required that the subsidiary deliver additional collateral on account of the changed financial condition of the covered financial company, the counterparty's right to exercise that remedy would be prohibited by the Final Rule and, accordingly, the counterparty would not be permitted to terminate or accelerate the contract based on the non-delivery by the subsidiary of the additional collateral.

The letter from the financial industry associations also requested that the Proposed Rule be revised to clarify that the contractual rights of a counterparty to demand performance from a subsidiary or affiliate of the covered financial company at any time and for any reason cannot be interfered with under section 210(c)(16), without inquiry "whether demand is made as a result of the CFC's default." The FDIC agrees that the rule is only intended to restrict the ability of a counterparty to take action based on the

insolvency, financial condition or receivership of the covered financial company. Thus, if contractual terms provide a counterparty with a right to require margin or repayment in full or other performance on demand, without any linkage to the covered financial company, the enforceability of the provision is not limited by the Final Rule. On the other hand, if a right to demand margin is premised on the existence of a condition that is financial in nature, such as the counterparty deeming itself insecure, and if the counterparty's demand is based upon the financial condition of the covered financial company, such demand would not be permitted by the Final Rule.

The financial industry association letter objected to the provisions of the Proposed Rule that would prevent a margin call against a subsidiary or affiliate of a covered financial company based on a change in the rating of the covered financial company following the appointment of the receiver. The letter argued that prohibiting such margin calls "goes beyond the statutory scope of section 210(c)(16), which only permits the FDIC to override contractual provisions to 'terminate, liquidate or accelerate.'" This argument seems to be a very narrow reading of the scope of section 210(c)(16). As discussed in more detail under *III. The Final Rule - Section-by-section analysis* below, a broader reading of the section is necessary to implement the intended effect of the Statute to limit the impact of changes in the financial condition of the covered financial company on contractual relationships of counterparties. Allowing unlimited margin calls would impede the orderly resolution of the covered financial company and may well have the same practical effect as the termination of the applicable subsidiary or affiliate contract.

This letter also objected that under the Proposed Rule it appeared that margin levels would be frozen based on the rating of the covered financial company immediately

before the receiver was appointed. The letter suggested that rights to margin under contracts supported by the covered financial company be based on the rating of the bridge financial company or other qualified transferee to which the support is transferred and that rights to margin on a contract of a subsidiary that is linked but not supported be based on the rating of the entity to which the direct or indirect ownership interests in such subsidiary have been transferred. This would not be consistent with section 210(c)(16), which refers to actions based on the financial condition of the covered financial company. This statutory framework is conducive to the creation of a period of stability following the appointment of a receiver to allow for the orderly resolution of a covered financial company. Moreover, it is not unlikely that ratings are uncertain in times of economic uncertainty; it is also likely that a bridge financial company would be unrated. The protection provided by section 210(c)(16) is particularly important with respect to remedies, such as margin calls, that if permitted to be asserted against a subsidiary or affiliate could impede the ability of the receiver to accomplish an orderly liquidation in a manner that minimizes the impact on the U.S. economy.

Although the counterparty's ability to call for additional margin would be suspended until the end of the orderly liquidation process to the extent that margin levels were based on the financial condition of the covered financial company, it should be noted that the Final Rule would not interfere with the operation of other contractual provisions that would result in changes in the level of collateral during the orderly liquidation process.

The financial industry association letter also asserted that section 210(c)(16) requires that adequate protection be provided for counterparties to contracts that are

linked to, but not supported or guaranteed by, the covered financial company. The FDIC does not find this position supported in the express language of the statute. The portion of section 210(c)(16) in question states that the FDIC as receiver shall have the power to enforce subsidiary or affiliate contracts, the obligations under which are guaranteed or otherwise supported or linked to the covered financial company, if "(i) such guaranty or other support and all related assets and liabilities are transferred to and assumed by a bridge financial company or a third party. . . or (ii) the Corporation, as receiver, otherwise provides adequate protection with respect to such obligations." Since the initial clause refers only to guaranty and support, the most straightforward reading is that each of the two clauses refers only to guaranties and other support and not to mere linkages that are not supported. The clause clearly intends to provide two alternatives for the circumstances that are intended to be covered – (i) the transfer of the guaranty or other support or (ii) the granting of adequate protection. Clause (i) is clearly directed only at guaranties and other support. If clause (ii) were construed to apply to other linked contracts, clause (ii) would be the only option for such contracts and would not work consistently with clause (i).

Moreover, the interpretation suggested by the commenter might serve to create a windfall for counterparties of subsidiaries or affiliates by requiring the creation of support when none originally existed. If, prior to the failure of the covered financial company, a linked contract were not supported by a guaranty or collateral provided by the covered financial company, the concept of adequate protection would not suggest a requirement for the creation of such support after the failure.

One of the letters from the insurance industry commenters also addressed linked-but-not supported contracts and objected to the Proposed Rule treating such contracts as covered by the Proposed Rule. The text of section 210(c)(16) specifically refers to a category of agreements that are "linked" to the covered financial company, in addition to agreements which are guaranteed or otherwise supported by the covered financial company. Accordingly, it is quite clear that contracts that are linked but not guaranteed or supported are included as protected contracts under section 210(c)(16).

This commenter also objected that the Proposed Rule exceeded the intended effect of section 210(c)(16) by providing the power to enforce subsidiary and affiliate contracts not only to the FDIC as receiver but also to transferees of the covered financial company, such as bridge financial companies and third party acquirers. While the FDIC does not view the provision in the Proposed Rule that would have granted such authority to a transferee as providing any significant powers that were not suggested by the text of section 210(c)(16), the extension of such authority to transferees is not necessary to achieve the purposes of section 210(c)(16) and has not been included in the Final Rule. As noted in *III. The Final Rule- Section-by section analysis* below, such contracts remain enforceable by the applicable subsidiary or affiliate as well as by the FDIC as receiver.

The financial industry association letter also expressed concern that setoff or netting rights in respect of qualified financial contracts could be impaired unless the Proposed Rule was revised to limit the scope of section 210(c)(16) by providing that qualified financial contracts of subsidiaries or affiliates of a covered financial company would be enforceable only to the extent that such enforcement does not impair setoff or netting rights with respect to other qualified financial contracts. The limitation sought

by the commenter generally was not consistent with the Statute. Moreover, in the examples provided in the letter, the asserted practical limitation on setoff or netting rights would result from the counterparty deciding to close out contracts, a situation wholly within the control of the counterparty.

The financial industry association letter also requested clarification of the terms "adequate protection" and "indubitable equivalent." As discussed below, it is intended that these terms be interpreted consistently with their treatment under the Bankruptcy Code. The letter correctly observes that under the Bankruptcy Code these terms are applied in the context of secured obligations and that they are subject to varying treatment among different jurisdictions and cases. Nonetheless, there is sufficient guidance in this precedent to provide at least a comparable degree of certainty in application as is provided by the Bankruptcy Code. The fact that under the Final Rule these terms are also to be applied to unsecured obligations should not detract from the guidance provided by such precedent.

The financial industry associations also requested that the option to provide cash payments as a form of adequate protection be clarified and that the difference between this option and option of providing a guaranty of the receiver be clarified. The option to provide cash payments was included for cases where a full guaranty by the receiver would provide a disproportionate benefit to a counterparty or where there might be other reasons why the FDIC might prefer the use of cash to a guaranty. Such a situation might arise, for example, where there was a limited guaranty in favor of the counterparty that was not transferred to a bridge financial company. Another situation would be where a portion of collateral supporting a counterparty obligation was not transferred. In each of

these cases, there might be an increased risk of loss to the counterparty arising from such failure to transfer, but the loss might be limited in nature.

The letter also stated that "[w]hile we believe that the FDIC means for 'adequate protection' to protect counterparties from any incremental loss sustained due to actions taken by the FDIC as receiver for a covered financial company, clarifying this view could help provide much-needed certainty with respect to the application of this term." As suggested above, this is not a correct reading of the Final Rule. With respect to contracts of subsidiaries and affiliates that the receiver desires to remain enforceable notwithstanding an applicable specified financial condition clause, adequate protection would be provided only to compensate for the increased risk of loss due to the non-transfer of all or any portion of the covered financial company's support for such contract or related assets and liabilities.

This letter also requested that the FDIC provide a procedure for counterparties to challenge the FDIC's adequate protection determinations. Such special procedures would be inconsistent with the urgency of the FDIC's responsibility to act expeditiously and efficiently in resolving a covered financial company. The Act makes clear that the FDIC as receiver should not be subject to delays of the type that are inherent in the bankruptcy process. For example, section 210(e) of the Act provides that no court may take any action to restrain or affect the exercise of powers or functions of the receiver.

The letters from the insurance industry included certain comments that relate only to the insurance industry. One letter proposed that the Final Rule state that section 210(c)(16) will not be applied to enforce a contract of an affiliate or subsidiary of a covered financial company if the affiliate or subsidiary is an insurance company. The

commenter argued that because the Act provides that an insurance company should be liquidated in accordance with state law, Congress intended that insurance company subsidiaries and affiliates of a covered financial company should not be subject to the orderly liquidation provisions of Title II. In fact, to the contrary, insurance companies are expressly included among financial companies that may, in the circumstances set forth in the Act, become covered financial companies.

Two insurance industry letters urged that the Final Rule include a provision that excludes director's or officer's liability insurance contracts and depository and financial institution bonds from the scope of the Final Rule. Both letters cited section 210(c)(13) of the Act, which specifically exempts liability insurance contracts and financial institution bonds entered into by a covered financial company from that section's general invalidation of *ipso facto* provisions, but both letters also noted that the Proposed Rule was not intended to override section 210(c)(13). One of these letters cited the "common practice of a parent financial institution including its affiliates or subsidiaries as insureds under its financial institution bond." The other letter argued that the Proposed Rule would override a "key historical element" of a director's or officer's liability insurance contract that allows an "automatic run-off" upon a change in control of the insured company. The FDIC agrees that if the bond or insurance contract is entered into with the covered financial company and not with the subsidiary or affiliate in question, pursuant to section 210(c)(13) the contract with the covered financial company would be terminable by the insurance company. Unlike the *ipso facto* provisions of the Act, however, section 210(c)(16) does not exempt director and officer liability policies. Rather, it applies to all contracts. Thus, if the obligations to the subsidiary or affiliate under the bond or

insurance contract constitute a contract between the insurance company and the subsidiary or affiliate, such obligations would not be covered by the exception to the *ipso facto* provisions of section 210(c)(13) and the contract with the subsidiary or affiliate would not be terminable by the insurance company upon the appointment of the receiver for the covered financial company. This is particularly important because the subsidiaries and affiliates are expected to include companies which will continue to operate and will need to have the protection afforded by this insurance.

One of the insurance industry letters also proposed that the definition of "support" be expanded to include support that is not financial in nature, such as an agreement by a covered financial company to provide specific performance of the obligations of a subsidiary or affiliate. The phrase "guaranteed or otherwise supported" in section 210(c)(16) strongly suggests that the reference to support is support that is financial in nature.

Finally, this letter also objected to the provision in the Proposed Rule that permits notice of the transfer of support and related assets and liabilities or the provision of adequate protection to be made on a website. As noted in the NPR, section 210(c)(16) does not require that any notice be given. However, the FDIC recognizes that counterparties will need to know the status of their contracts and the website posting option is included in the Final Rule in acknowledgement of the public's growing reliance on internet communication as well as the prevalence of online commerce. The Final Rule permits such posting in order to provide a means for the giving of notice that is practical from the perspective of the receiver, which might otherwise be burdened with having to send many thousands of notices, as well as from the perspective of the parties

to the applicable contracts with the subsidiaries and affiliates, which would ordinarily be expected to monitor public information relating to covered financial companies and their subsidiaries and affiliates. The FDIC believes that the notice provisions of the Final Rule are reasonably calculated to provide actual notice.

III. The Final Rule

Overview

The Final Rule clarifies that the power of the Corporation as receiver to enforce contracts of subsidiaries and affiliates under Dodd-Frank Act section 210(c)(16) effectively preserves contractual relationships of subsidiaries and affiliates of the covered financial company during the orderly liquidation process. The Final Rule identifies certain contracts that are "linked to" the covered financial company within the meaning of the Statute, as well as contracts that also are "supported by" the covered financial company. Under the Statute, a contract is "linked to" a covered financial company if it contains a provision that provides a contractual right to "cause the termination, liquidation or acceleration of such contract based solely on the insolvency, financial condition, or receivership of the covered financial company." That type of provision, called a "specified financial condition clause" in the Final Rule, is more fully defined in the Final Rule. Although the Statute speaks in terms of the power to enforce a contract to which the receiver is not a party, the Final Rule recognizes the practical effect of this authority, which is that the counterparty to such a contract may not exercise remedies in connection with a specified financial condition clause if the statutory conditions are met. No action is required of the receiver to enforce a linked contract; the Final Rule makes

clear that the contract will remain in full force and effect unless the receiver fails to meet the requirements with respect to any supporting obligations of the covered financial company.

The Final Rule establishes that if the subsidiary's obligations under the linked contract are supported by the covered financial company through, for example, guaranties or the granting of collateral that supports the obligations, the Corporation as receiver must either (a) transfer such support (along with all related assets and liabilities) to a qualified transferee not later than 5:00 p.m. (eastern time) on the business day following the appointment of the receiver, or (b) provide "adequate protection" to contract counterparties following notice given to the counterparties in accordance with the guidelines set forth in the Final Rule by the one-business-day deadline.

The Final Rule also clarifies the meaning of the statutory provision regarding a contractual obligation that is "guaranteed or otherwise supported by" the covered financial company. Support includes guaranties that may or may not be collateralized and other examples of financial support of the obligations of the subsidiary or affiliate under the contract. In circumstances where a contract of a subsidiary or affiliate is linked to the financial condition of the parent company via a "specified financial condition clause," but where the obligations of the subsidiary or affiliate are not "supported by" the covered financial company through guaranties or similar supporting obligations, the requirement to transfer support and related assets or provide adequate protection does not apply. The mere existence of a "specified financial condition clause" does not constitute a "support" obligation by the covered financial company, and the Final Rule makes it clear that the subsidiary or affiliate contract remains enforceable without any requirement to effectively

create new support where none originally existed. This is consistent with the effect of section 210(c)(13), providing that *ipso facto* clauses in contracts of the covered financial company are unenforceable, and section 210(c)(8) of the Dodd-Frank Act, providing that "walkaway clauses" in qualified financial contracts of the covered financial company are unenforceable. In the case of those types of contractual provisions, there is no specified entity required to provide support, hence the concept of alternate support or adequate protection is inapplicable. In the same way, under the Final Rule, the concept of adequate protection does not arise in the absence of supporting obligations by the specified entity.

The Final Rule applies broadly to all contracts, and not solely to qualified financial contracts. For example, a real estate lease or a credit agreement, neither of which would typically be classified as a qualified financial contract, is subject to enforcement under section 210(c)(16) and the Final Rule notwithstanding a specified financial condition clause that might, for instance, give a lessor the right to terminate a lease based upon a change in financial condition of the parent of the lessee. A swap agreement of a subsidiary or affiliate is subject to section 210(c)(16) and the Final Rule in the same manner if the agreement contains specified financial condition clause.

The Final Rule does not affect other provisions of the Dodd-Frank Act governing qualified financial contracts, such as sections 210(c)(8) ("Certain Qualified Financial Contracts") and 210(c)(9) ("Transfer of Qualified Financial Contracts"). For example, where a covered financial company's support of a subsidiary or affiliate obligation would itself be considered a qualified financial contract, such as a securities contract, the provisions of section 210(c)(9) that prohibit the selective transfer of qualified financial

contracts with a common counterparty (or a group of affiliated counterparties) continue to apply. Likewise, the provisions in section 210(c)(10) of the Dodd-Frank Act applicable to counterparties of qualified financial contracts also continue to apply. On the other hand, if the covered financial company's support of a subsidiary or affiliate consists of multiple contracts that are not qualified financial contracts, the Corporation as receiver may transfer all or a portion of such group of contracts as long as it provides adequate protection for the supporting obligations that were not transferred. Similarly, the Corporation may transfer all or a portion of "related assets and liabilities" that are not qualified financial contracts if it provides adequate protection for the portion of the assets and liabilities that was retained by the Corporation as receiver.

Section-by-section analysis.

Paragraph (a) of the Final Rule states the general rule with respect to the authority granted under section 210(c)(16) of the Dodd-Frank Act, i.e., that the contracts of a subsidiary or affiliate of a covered financial company are enforceable notwithstanding the existence of a "specified financial condition clause" that provides a counterparty with the right to terminate or exercise remedies based upon the financial condition of the parent or affiliate covered financial company, provided that the FDIC as receiver for the covered financial company transfers all support and related assets and liabilities that back the obligations of such subsidiary or affiliate. To the extent that the receiver fails to transfer all support and related assets and liabilities, it must provide adequate protection to such counterparty to preserve its right to enforce the contracts of the subsidiary. The effect of this ability to enforce the contract is intended to be broad enough to preclude the counterparties from terminating or exercising other remedies such as requiring additional

collateral but is intended to be limited in scope solely to remedies arising out of a specified financial condition clause, not other contractual defaults by the subsidiary or affiliate. The ability either to transfer support or to provide adequate protection can be exercised in the alternative, or in combination. For example, if some, but not all collateral is transferred, appropriate adequate protection may be provided in lieu of the collateral not transferred.

The deadline for the transfer of support is the same as the time limit applicable to the transfer of qualified financial contracts under section 210(c)(10) of the Dodd-Frank Act, i.e., by 5:00 p.m. (eastern time) on the next business day. Although the decision to provide adequate protection in lieu of transferring support must also be made and steps must be taken that are reasonably calculated to provide notice within a business day, the language of the Final Rule does not require that the adequate protection be fully in place by that next-day deadline. Although the failure to complete within a business day the necessary documentation or transactions should not be deemed to be a waiver of the right to enforce the contract, once the receiver has provided notice of its intent to transfer support or provide adequate protection, the counterparty would be entitled to the benefit of the support or adequate protection even if the need for access to such support or protection arises before the applicable documentation or transfer of collateral is fully completed.

The Final Rule provides, as set forth in the Statute, that the Corporation as receiver has the authority to enforce linked contracts under the section 210(c)(16) of the Dodd-Frank Act. Also, the subsidiary or affiliate continues to have the ability to enforce the terms of such contracts as well. In essence, the effect of such authority to enforce is

substantively the same as a prohibition of the counterparty to assert a specified financial condition clause against the subsidiary or affiliate. Effectively, the Final Rule makes clear that the practical effect of the operation of section 210(c)(16) is similar to that of section 210(c)(13) (prohibiting counterparties from the exercise of certain rights arising out of *ipso facto* clauses) and section 210(c)(8)(F) (prohibiting counterparties to qualified financial contracts from the exercise of certain rights arising out of walkaway clauses); i.e., that the counterparties are prohibited from exercising remedies under a specified financial condition clause if the statutory conditions are met.

Section 210(c)(16) expressly states that the power to enforce contracts of a subsidiary in the circumstances described in the Statute is vested in "[t]he Corporation, as receiver for a covered financial company or as receiver for a subsidiary of a covered financial company (including an insured depository institution)." This is captured in section 380.12(a)(3) of the Final Rule. This recognizes that the preservation of value through the enforcement of subsidiary and affiliate contracts is important to all of the interconnected entities that are related to the entity in receivership. The effect of the Statute is to prohibit the counterparty from terminating or exercising remedies based solely on the financial condition of the covered financial company. Once the essential link to the covered financial company is established via the specified financial condition clause, the contract is enforceable by the receiver and by the subsidiary or affiliate that is the direct party-in-interest to the contract.

Definitions

Section 380.1 is revised in the Final Rule because four terms have been added to it. These terms – "subsidiary," "affiliate," "control" and "business day" – are used in the

Final Rule but have been included as defined terms under section 380.1 because they are, or may be, used on more than one occasion in part 380. One of these terms – "business day" – was not included in the Proposed Rule but is defined in Title II of the Act. The other terms were included in the *Definitions* section of the Proposed Rule.

The Final Rule includes six definitions in its *Definitions* section: "linked," "specified financial condition clause," "support," "related assets and liabilities," "qualified transferee" and "successor" that relate specifically to the matters discussed in the Final Rule and therefore are not included in section 380.1 among definitions of general applicability to Part 380.

A contract is "**linked**" to a covered financial company if it contains a specified financial condition clause naming the covered financial company as the specified company.

The term "**specified financial condition clause**" is intended to broadly capture any provision that gives any counterparty a right to terminate, accelerate or exercise default rights or remedies as a result of any action or circumstance that results in or arises out of the exercise of the orderly liquidation authority. Each aspect of the definition of the term "specified financial condition clause" should be read expansively so that counterparties are effectively stayed from exercising rights under such a clause to terminate contracts or exercise other remedies during a Title II resolution process if the requirements of the Statute are met. Thus, a specified financial condition clause includes any clause that might be interpreted as giving rise to a termination right or other remedy due to the insolvency of the specified covered financial company that might have precipitated the appointment of the receiver, such as an act of insolvency or a downgrade

in a rating from a rating agency. Likewise, as indicated in the NPR, the definition is broad enough to include a change in control provision that creates termination rights or other remedies upon the appointment of the FDIC as receiver or other change in control, such as the transfer of stock in the subsidiary to the bridge financial company or the sale, conversion or merger of the bridge financial company or its assets or the issuance of interests in the bridge financial company or its successor to creditors of the covered financial company in satisfaction of their claims. As stated in the NPR, the intent is to allow the subsidiary or affiliate contract to remain in effect despite the exercise of any or all of the authorities granted to the FDIC as receiver for a covered financial company throughout the orderly liquidation process.

Although the language of the Statute refers to the counterparty's rights as "termination, liquidation or acceleration," that list of remedies cannot be read to be exclusive, as the purpose of the provision is provide the FDIC with the power it needs to preserve going-concern value of the covered financial company as long as the rights of counterparties to receive bargained-for support is respected. Accordingly, the Final Rule uses the broader phrase "terminate, liquidate, accelerate or declare a default under" the contract. In effect, the specified financial condition clause is unenforceable if the statutory requirements are met. In addition, by clarifying that the link created by the specified financial condition clause may operate "directly or indirectly," the Final Rule clarifies that the scope of the defined term includes contracts where the specified company under the clause may be another company or an affiliate in the corporate structure so long as the ultimate triggering event relates to the financial condition of the covered financial company or the Title II actions taken with respect to that covered

financial company. The term "specified company" used in the definition is consistent with terminology commonly used in such provisions in derivatives contracts to refer to the company whose financial condition is the basis for the termination right or other remedy.

Language in this definition is borrowed from sections of the Dodd-Frank Act addressing related matters, such as the enforceability of contracts of the covered financial company notwithstanding *ipso facto* clauses (section 210(c)(13)) and walkaway clauses with respect to qualified financial contracts (section 210(c)(8)(F)). The fact that this language is adapted and expanded upon should not be deemed to reflect any interpretation of the meaning or possible limitations of those sections. The broad language of this definition reflects the authority granted in section 210(c)(16), which ensures that the receiver has the power to avoid precipitous terminations by counterparties of the subsidiary resulting in disorderly collapse and a loss of value to the covered financial company.

In the event a counterparty (including its affiliates) has more than one contract with the subsidiary or affiliate of the covered financial company, any contract with a cross-default provision with respect to another contract containing a specified financial condition clause also would be "linked." The same would be true of a single contract of a counterparty with a subsidiary or affiliate that cross-defaulted to the contract of another subsidiary or affiliate that contained a specified financial condition clause.

In order to make unmistakably clear that, as set forth in the Proposed Rule, section 210(c)(16) and the Final Rule protect covered contracts of subsidiaries and affiliates from the exercise of remedies until completion of the resolution process, a new

subclause (G) has been added to specifically refer to a step that may be taken in the resolution process by the successor to a bridge financial company. The listed steps are intended to be illustrative but not exclusive. As stated in the NPR, section 210(c)(16) and the Final Rule give the receiver the necessary tools to keep subsidiary and affiliate contracts with specified financial condition clauses in place throughout the resolution process. This is further discussed below in the description of the definition of "successor."

The term "**support**" means to guarantee, indemnify, undertake to make any loan, advance or capital contribution, maintain the net worth of the subsidiary or affiliate, or provide other financial assistance. This would include a pledge of collateral that directly secures an obligation of a subsidiary or affiliate. The definition does not include other assistance that is not financial in nature, such as an undertaking to conduct specific performance. Generally, if the obligation of the counterparty to perform is linked to the financial condition of the parent, the support also would likely be financial, and other types of arrangements are beyond the scope of the Statute. One comment was received in response to a question included in the NPR as to the sufficiency of this definition. As noted under *II. Summary of Comments on the Proposed Rule* above, this commenter argued that the definition should be expanded to include support that is not financial in nature. However, including such type of support in the definition would be inconsistent with section 210(c)(16).

The term "**related assets and liabilities**" includes assets of the covered financial company serving as collateral securing the covered financial company's support obligation, and setoff rights or netting arrangements to which the covered financial

company is subject if they are related to the covered financial company's support. It should be noted, however, that if the "support" were in the nature of a guaranty, the related assets and liabilities would not consist of all of the assets of the covered financial company unless the guaranty was secured by all assets of the covered financial company. The transfer of an unsecured guaranty or obligation to a qualified transferee would meet the requirements of the Final Rule in this regard, without the transfer of any particular assets. The definition also broadly includes any liabilities of the covered financial company that directly arise out of or relate to its support of the obligations or liabilities of the subsidiary or affiliate. In some instances, this definition may be redundant with the definition of support, as a guaranty could be both a related liability and a supporting obligation. The broader definition is intended to make clear that the full range of supporting obligations and related assets and liabilities must be transferred to ensure that the counterparties are in substantially the same position as they were prior to the transfer to the qualified transferee.

It is important to note that in some situations "support" and "related assets and liabilities" are themselves qualified financial contracts. Section 210(c)(8)(D)(ii)(XII) of the Act includes "securities contracts" as qualified financial contracts, and defines securities contracts to include "any security agreement or arrangement or other credit enhancement related to any agreement or transaction referred to in this clause, including any guaranty or reimbursement obligation in connection with any agreement or transaction referred to in this clause." Other types of qualified financial contracts, such as for example, swaps (in section 210(c)(8)(D)(vi)(VI) of the Act), are similarly defined to include related security agreements arrangements and other credit enhancements. To

the extent such support and related assets and liabilities themselves constitute financial contracts, they are subject to the rules applicable to the treatment of qualified financial contracts, including the so-called all-or-none rule under section 210(c)(9).

The term "**qualified transferee**" specifically includes a bridge financial company as well as any unrelated third party (other than a third party for which a conservator, receiver, trustee in bankruptcy, or other legal custodian has been appointed, or which is otherwise the subject of a bankruptcy or insolvency proceeding). A qualified transferee can include both the bridge financial company and a subsequent transferee; for instance, if assets and liabilities, including the support and related assets and liabilities are transferred first to a bridge financial company and then to another acquirer either prior to or upon the termination of the bridge financial company pursuant to the orderly liquidation authorities granted under Title II of the Dodd-Frank Act.

The definition of the terms "**subsidiary**" and "**affiliate**" are consistent with the definitions given to such terms in the Dodd-Frank Act. Section 2(18) of the Act, codified at 12 U.S.C. 5301(18), provides that these terms will have the same meanings as in section 3 of the FDI Act (12 U.S.C. 1813). Under the Federal Deposit Insurance Act ("FDI Act"), the term "subsidiary" is broadly defined as "any company which is owned or controlled directly or indirectly by another company…." "Affiliate" is defined by reference to the Bank Holding Company Act, 12 U.S.C. 1841(k) as "any company that controls, is controlled by, or is under common control with another company."

The term "**control**" is used in the definitions of the terms "subsidiary" and "affiliate." The Statute refers to the definition of "control" provided in the FDI Act, which in turn, refers to the definition provided in the Bank Holding Company Act, 12

U.S.C. 1841(a). In defining the use of this term for purposes of the definitions of "subsidiary" and "affiliate," the Final Rule streamlines these cross-references, clarifies that certain provisions of the Bank Holding Company Act definition are inapplicable in this context, and adopts the flexible approach of conforming to the relevant provisions of the Bank Holding Company Act and regulations promulgated thereunder at the time of appointment of the receiver.

In effect, the definition of "control" includes, as a company in "control" of another company, a company that directly or indirectly or acting through one or more persons owns, controls, or has the power to vote 25 percent or more of any class of voting securities of the other company. Under the Final Rule, a company may also exercise "control" if that company controls in any manner the election of a majority of the directors or trustees of the company. This definition is consistent with the Bank Holding Company Act definition as it has been reflected in regulations promulgated under that section, including Regulation W (12 C.F.R. 223.3(g)) and Regulation Y (12 C.F.R. 225.2(e)).

Section 2 of the Dodd-Frank Act expressly adopts the FDI Act definitions that incorporate the Bank Holding Company Act definitions "except to the extent the context otherwise requires." Parts of the Bank Holding Company Act definition of "control" are inapposite to the context of section 210(c)(16). Provisions that provide for a determination of "control" made by the Federal Reserve Board of Governors pursuant to a notice and hearing are inconsistent with the expedited decision-making expressly required by section 210(c)(16).

An entity is deemed to be a "**successor**" of a bridge financial company if it is the company into which the bridge financial company is converted by way of incorporation under the laws of a state or if it is the surviving company of a merger or consolidation of the bridge financial company with another company (whether before or after any such conversion). Although this definition was not included in the Proposed Rule, no substantive change is effected by its insertion in the Final Rule. Under the Act, it is possible that a bridge financial company's status as such could terminate before the resolution process is completed and a successor merely constitutes a continuation of a qualified transferee. By including this definition for "successor," the Final Rule more specifically reflects a possible step and strategy in the resolution process that, while clearly within the general scope of the Proposed Rule and NPR, was not given specific mention.

The term "**business day**" is defined in the same way such term is defined in section 210(c)(10)(D) of the Act, relating to notification of transfer of qualified financial contracts. This is consistent with the notice requirement in the Final Rule, which provides for steps to be taken to provide notice during the same time period that is applicable for the taking of steps to provide notice of the transfer of qualified financial contracts. This was also contemplated by a question included in the NPR (in respect of which no responses were received) as to whether "business day" should be defined consistently with the definition in section 210(c)(10)(D).

Adequate Protection

Paragraph (c) of the Final Rule describes the different ways that the Corporation may provide adequate protection in the event that it does not transfer a covered financial

company's support to a qualified transferee. The definition of adequate protection is consistent with the definition in section 361 of the Bankruptcy Code[1], which also formed the basis of the definition of adequate protection in the context of treatment of certain secured creditors under 12 C.F.R. 380.52. Adequate protection may include any of the following: (1) making a cash payment or periodic cash payments to the counterparties of the contract to the extent that the failure to cause the assignment and assumption of the covered financial company's support and related assets and liabilities causes a loss to the counterparties; (2) providing to the counterparties a guarantee, issued by the Corporation as receiver for the covered financial company, of the obligations of the subsidiary or affiliate of the covered financial company under the contract; or (3) providing relief that will result in the realization by the claimant of the indubitable equivalent of the covered financial company's support. The phrase "indubitable equivalent," which appears in section 361 of the Bankruptcy Code, is intended to have a meaning consistent with its meaning in bankruptcy, in conformance with section 209 of the Dodd-Frank Act that requires rules promulgated under Title II of the Act to be "harmonized" with the Bankruptcy Code where possible. One comment was received requesting further clarification of the definitions of adequate protection and indubitable equivalent. As discussed under *II. Summary of Comments on the Proposed Rule* above, no further clarification of these terms was deemed necessary.

It is important to note that although a guaranty of the Corporation as receiver is expressly included among the enumerated examples of "adequate protection" in paragraph (c) of the Final Rule, the omission of such specific reference in 12 C.F.R.

[1] 11 U.S.C. § 361.

380.52 is not intended to suggest that such a guaranty would not constitute adequate protection to secured creditors under to 12 C.F.R. 380.52. The guaranty of the receiver is, in any event, the indubitable equivalent of any guaranty or support that it may replace, and the express mention of the guaranty is added only for the avoidance of any doubt. Any such guaranty issued in accordance with the Act would be backed by the assets of the covered financial company, and also would be supported by the orderly liquidation fund and the authority of the Corporation as manager of the orderly liquidation fund to assess the financial industry pursuant to section 210(o) of the Act. Such a guaranty would in all events qualify as the indubitable equivalent of any guaranty or support that it may replace. The express mention of the guaranty is added merely for the avoidance of any doubt.

Notice of Transfer or Provision of Adequate Protection

Paragraph (d) of the Final Rule provides that if the Corporation as receiver transfers any support and related assets and liabilities of the covered financial company or decides to provide adequate protection in accordance with subparagraphs (a)(1) and (2), it will promptly take steps to notify contract counterparties of such transfer or provision of adequate protection. Although the Statute does not contain a notice requirement, the Final Rule requires that these reasonable steps be taken to provide notice in recognition of the practical reality that contract counterparties will need to know whether they may exercise remedies under a specified financial condition clause. In acknowledgement of the public's growing reliance on internet communication as well as the prevalence of online commerce, the Final Rule provides that the Corporation may post such notice on its public website, the website of the covered financial company or

the subsidiary or affiliate, or provide notice via other electronic media. One comment was received in response to the question posed by the NPR as to whether these steps were reasonably calculated to provide notice. This commenter objected that navigation of websites is often difficult and that counterparties may not be aware that the parent financial company was placed into receivership and that, accordingly, this form of notice was inadequate. As discussed under *II. Summary of Comments on the Proposed Rule* above, no change has been made in the Final Rule. The use of electronic notification is effective and efficient in connection with the failure of a systemically important financial company. In such a case, individually directed notice would be unduly cumbersome and burdensome.

While the Corporation will endeavor to provide notice in a manner reasonably calculated to provide notification to the parties in a timely manner, the provision of actual notice is not a condition precedent to enforcing such contracts. Any action by a counterparty in contravention of section 210(c)(16) will be ineffective, whether or not such counterparty had actual notice of the transfer of support or provision of adequate protection. Further, where the contract of the subsidiary or affiliate is linked to the covered financial company but not otherwise supported by the covered financial company, actual notice of by the Corporation of its appointment as receiver or its intent to exercise the authority under section 210(c)(16) is not required.

IV. Regulatory Analysis and Procedure

A. Paperwork Reduction Act

In accordance with the Paperwork Reduction Act (44 U.S.C. § 3501, *et seq.*) ("PRA"), the FDIC may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid Office of Management and Budget (OMB) control number. The Final Rule would not involve any new collections of information pursuant to the Paperwork Reduction Act (44 U.S.C. § 3501, *et seq.*). Consequently, no information will be submitted to the Office of Management and Budget for review.

B. Regulatory Flexibility Act

The Regulatory Flexibility Act 5 U.S.C. § 601, *et seq.* (RFA) requires each federal agency to prepare a final regulatory flexibility analysis in connection with the promulgation of a final rule, or certify that the final rule will not have a significant economic impact on a substantial number of small entities.[2] Pursuant to section 605(b) of the Regulatory Flexibility Act, the FDIC certifies that the Final Rule will not have a significant economic impact on a substantial number of small entities.

C. Small Business Regulatory Enforcement Act

[Awaiting OMB determination]

[2] *See* 5 U.S.C. 603, 604 and 605.

D. The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The FDIC has determined that the Final Rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, enacted as part of the Omnibus Consolidated and Emergency Supplemental Appropriations Act of 1999 (Pub. L. 105–277, 112 Stat. 2681).

E. Plain Language

Section 722 of the Gramm-Leach-Bliley Act (Pub. L. 106–102, 113 Stat.1338, 1471), requires the Federal banking agencies to use plain language in all proposed and final rules published after January 1, 2000. The FDIC has sought to present the Final Rule in a simple and straightforward manner.

List of Subjects in 12 CFR Part 380

Banks, banking, Financial companies, Holding companies, Insurance companies, Mutual insurance holding companies.

For the reasons stated above, the Board of Directors of the Federal Deposit Insurance Corporation amends part 380 of title 12 of the Code of Federal Regulations as follows:

PART 380—ORDERLY LIQUIDATION AUTHORITY

■ 1. The authority citation for part 380 is revised to read as follows:

Authority: 12 U.S.C. 5383(e); 12 U.S.C. 5389; 12 U.S.C. 5390(c)(16); 12 U.S.C. 5390(s)(3); 12 U.S.C. 5390(b)(1)(C); 12 U.S.C. 5390(a)(7)(D).

■ 2. The heading for subpart A is revised to read as follows:

Subpart A—General and Miscellaneous Provisions

Sec.

380.1 Definitions.

380.2 [Reserved]

380.3 Treatment of personal service agreements.

380.4 [Reserved]

380.5 Treatment of covered financial companies that are subsidiaries of insurance companies.

380.6 Limitation on liens on assets of covered financial companies that are insurance companies or covered subsidiaries of insurance companies.

380.7 Recoupment of compensation from senior executives and directors.

380.8 [Reserved]

380.9 Treatment of fraudulent and preferential transfers.

380.10 Calculation of maximum obligation limitation.

380.11 Treatment of mutual insurance holding companies.

380.12 Enforcement of subsidiary and affiliate contracts by the FDIC as receiver of a covered financial company.

380.13–380.19 [Reserved]

■ 3. Amend § 380.1 by adding definitions of affiliate, business day, control and subsidiary in alphabetical order to read as follows:

§ 380.1 Definitions

Affiliate. The term "affiliate" means any company that controls, is controlled by, or is under common control with another company at the time of, or immediately prior to, the appointment of receiver of the covered financial company.

Business day. The term "business day" means any day other than any Saturday, Sunday or any day on which either the New York Stock Exchange or the Federal Reserve Bank of New York is closed.

Control. The term "control", when used in the definitions of "affiliate" and "subsidiary", has the meaning given to such term under 12 U.S.C. 1841(a)(2)(A) and (B) as such law, or any successor, may be in effect at the date of the appointment of the receiver, together with any regulations promulgated thereunder then in effect.

Subsidiary. The term "subsidiary" means any company which is controlled by another company at the time of, or immediately prior to, the appointment of receiver of the covered financial company.

■ 4. Revise § 380.12 to read as follows:

§ 380.12 **Enforcement of subsidiary and affiliate contracts by the FDIC as receiver of a covered financial company**.

(a) *General.*

(1) Contracts of subsidiaries or affiliates of a covered financial company that are linked to or supported by the covered financial company shall remain in full force and effect notwithstanding any specified financial condition clause contained in such contract and no counterparty shall be entitled to terminate, accelerate, liquidate or exercise any other remedy arising solely by reason of such specified financial condition clause. The Corporation as receiver for the covered financial company shall have the power to enforce such contracts according to their terms.

(2) Notwithstanding paragraph (a)(1) of this section, if the obligations under such contract are supported by the covered financial company then such contract shall be enforceable only if –

(i) Any such support together with all related assets and liabilities are transferred to and assumed by a qualified transferee not later than 5:00 p.m. (eastern time) on the business day following the date of appointment of the Corporation as receiver for the covered financial company; or

(ii) If and to the extent paragraph (a)(2)(i) of this section is not satisfied, the Corporation as receiver otherwise provides adequate protection to the counterparties to such contracts with respect to the covered financial company's support of the obligations or liabilities of the subsidiary or affiliate and provides notice consistent with the requirements of paragraph (d) of this section not later than 5:00 p.m. (eastern time) on the business day following the date of appointment of the Corporation as receiver.

(3) The Corporation as receiver of a subsidiary of a covered financial company (including a failed insured depository institution that is a subsidiary of a covered financial company) may enforce any contract that is enforceable by the Corporation as receiver for a covered financial company under paragraphs (a)(1) and (a)(2) of this section.

(b) *Definitions*. For purposes of this part, the following terms shall have the meanings set forth below:

(1) A contract is "linked" to a covered financial company if it contains a specified financial condition clause that specifies the covered financial company.

(2) (i) A "specified financial condition clause" means any provision of any contract (whether expressly stated in the contract or incorporated by reference to any other contract, agreement or document) that permits a contract counterparty to terminate, accelerate, liquidate or exercise any other remedy under any contract to which the subsidiary or affiliate is a party or to obtain possession or exercise control over any property of the subsidiary or affiliate or affect any contractual rights of the subsidiary or affiliate directly or indirectly based upon or by reason of

(A) A change in the financial condition or the insolvency of a specified company that is a covered financial company;

(B) The appointment of the FDIC as receiver for the specified company or any actions incidental thereto including, without limitation, the filing of a petition seeking judicial action with respect to the appointment of the Corporation as receiver for the

specified company or the issuance of recommendations or determinations of systemic risk;

(C) The exercise of rights or powers by the Corporation as receiver for the specified company, including, without limitation, the appointment of the Securities Investor Protection Corporation (SIPC) as trustee in the case of a specified company that is a covered broker-dealer and the exercise by SIPC of all of its rights and powers as trustee;

(D) The transfer of assets or liabilities to a bridge financial company or other qualified transferee;

(E) Any actions taken by the FDIC as receiver for the specified company to effectuate the liquidation of the specified company;

(F) Any actions taken by or on behalf of the bridge financial company to operate and terminate the bridge financial company including the dissolution, conversion, merger or termination of a bridge financial company or actions incidental or related thereto; or

(G) The transfer of assets or interests in a transferee bridge financial company or its successor in full or partial satisfaction of creditors' claims against the covered financial company.

(ii) Without limiting the general language of paragraphs (b)(1) and (b)(2) of this section, a specified financial condition clause includes a "walkaway clause" as defined in 12 U.S.C. 5390(c)(8)(F)(iii) or any regulations promulgated thereunder.

(3) The term "support" means undertaking any of the following for the purpose of supporting the contractual obligations of a subsidiary or affiliate of a covered financial company for the benefit of a counterparty to a linked contract --

(i) To guarantee, indemnify, undertake to make any loan or advance to or on behalf of the subsidiary or affiliate;

(ii) To undertake to make capital contributions to the subsidiary or affiliate; or

(iii) To be contractually obligated to provide any other financial assistance to the subsidiary or affiliate.

(4) The term "related assets and liabilities" means—

(i) Any assets of the covered financial company that directly serve as collateral for the covered financial company's support (including a perfected security interest therein or equivalent under applicable law);

(ii) Any rights of offset or setoff or netting arrangements that directly arise out of or directly relate to the covered financial company's support of the obligations or liabilities of its subsidiary or affiliate; and

(iii) Any liabilities of the covered financial company that directly arise out of or directly relate to its support of the obligations or liabilities of the subsidiary or affiliate.

(5) A "qualified transferee" means any bridge financial company or any third party (other than a third party for which a conservator, receiver, trustee in bankruptcy, or

other legal custodian has been appointed, or which is otherwise the subject of a bankruptcy or insolvency proceeding).

(6) A "successor" of a bridge financial company means

(i) A company into which the bridge financial company is converted by way of incorporation under the laws of a State of the United States; or

(ii) The surviving company of a merger or consolidation of the bridge financial company with another company (whether before or after the conversion (if any) of the bridge financial company).

(c) Adequate Protection.

The Corporation as receiver for a covered financial company may provide adequate protection with respect to a covered financial company's support of the obligations and liabilities of a subsidiary or an affiliate pursuant to paragraph (a)(2)(ii) of this section by any of the following means:

(1) Making a cash payment or periodic cash payments to the counterparties of the contract to the extent that the failure to cause the assignment and assumption of the covered financial company's support and related assets and liabilities causes a loss to the counterparties;

(2) Providing to the counterparties a guaranty, issued by the Corporation as receiver for the covered financial company, of the obligations of the subsidiary or affiliate of the covered financial company under the contract; or

(3) Providing relief that will result in the realization by the counterparty of the indubitable equivalent of the covered financial company's support of such obligations or liabilities.

(d) Notice of Transfer of Support or Provision of Adequate Protection.

If the Corporation as receiver for a covered financial company transfers any support and related assets and liabilities of the covered financial company in accordance with paragraph (a)(2)(i) of this section or provides adequate protection in accordance with paragraph (a)(2)(ii) of this section, it shall promptly take steps to notify contract counterparties of such transfer or provision of adequate protection. Notice shall be given in a manner reasonably calculated to provide notification in a timely manner, including, but not limited to, notice posted on the website of the Corporation, the covered financial company or the subsidiary or affiliate, notice via electronic media, or notice by publication. Neither the failure to provide actual notice to any party nor the lack of actual knowledge on the part of any party shall affect the authority of the Corporation to enforce any contract or exercise any rights or powers under this section.

Dated at Washington, D.C., this [Date].

By order of the Board of Directors.

Federal Deposit Insurance Corporation.

Robert E. Feldman,
Executive Secretary