

May 19, 2009

MEMORANDUM: The Board of Directors

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SUBJECT: Final Rule Providing for Modification of Temporary Liquidity
Guarantee Program to FDIC Guarantee Mandatory Convertible
Debt

I. SUMMARY OF RECOMMENDATIONS

Staff recommends that the Board adopt and authorize publication in the *Federal Register* of the attached Final Rule. The Final Rule would effect a targeted modification of the debt guarantee program (DGP) to permit the FDIC to guarantee certain mandatory convertible debt (MCD) of any entity participating in the DGP that applies to and receives approval from the FDIC to issue such MCD. Staff expects the Final Rule to provide such entities the flexibility needed to obtain funding from investors that may have a longer-term investment horizon, and moderate any refinancing risk that may arise upon the expiration of the FDIC guarantee in 2012.

Discussion

The TLGP is part of a multifaceted effort by the FDIC, the United States Department of the Treasury, and the Board of Governors of the Federal Reserve System

(Federal Reserve) to address unprecedented disruptions in credit markets and the resultant effects on the ability of financial institutions to fund themselves and to make loans to creditworthy borrowers. The TLGP and other government programs have had favorable effects thus far; however, the FDIC continues to evaluate ways to make the TLGP more effective.

On February 27, 2009 the Board approved an Interim Rule that modified the DGP to permit the FDIC to guarantee certain MCD of any entity participating in the DGP that receives approval from the FDIC to issue MCD.¹ Applications to issue MCD must provide the details of the request (including the proposed amount, issue date, and conversion rate), a summary of the applicant's strategic operating plan, and a description of the proposed use of the debt proceeds.² The deadline for filing applications to issue MCD is October 31, 2009 for insured depository institutions and certain participating entities for which the DGP is extended; otherwise, the deadline is June 30, 2009.

To qualify for the FDIC's guarantee, MCD must satisfy the requirements provided for senior unsecured debt under the DGP. Approval to issue MCD does not affect the debt guarantee limit of the issuing entity. The assessment fee for the FDIC's guarantee of MCD is based on the time from the date of the issue until the mandatory conversion date.

The intent of the Rule was to provide the flexibility needed to obtain funding from investors with longer-term investment horizons, and reduce amount of debt that

¹ See 74 FR 9522 (March 4, 2009).

² Where the issuance of MCD could potentially raise control issues, the applicant seeking to issue FDIC-guaranteed MCD also must provide confirmation that its appropriate Federal banking agency has received all applications and all notices or approvals required under the Bank Holding Company Act of 1956, as amended, the Home Owners' Loan Act, as amended, or the Change in Bank Control Act, as amended, in order to issue the debt.

participating entities may need to refinance or replace when the FDIC guarantee expires in 2012.

The FDIC received eight public comments on the Interim Rule from banks, trade and industry groups, and certain individuals. The commenters generally supported the Interim Rule in that it would provide participating entities the flexibility needed to attract a broader group of investors, including those with longer-term investment horizons. Some commenters sought clarification on the scope of coverage of the FDIC's guarantee in the event of the bankruptcy or receivership of the issuing entity. In addition, as discussed in the *Federal Register* document, other commenters encouraged the FDIC to revise the TLGP in a way that would permit eligible entities to use the DGP for purposes of raising capital, and by eliminating the prior application requirement for issuing MCD and providing more flexibility for purposes of establishing debt guarantee limits.

Final Rule

The Final Rule is generally consistent with the Interim Rule; however, certain revisions were made to clarify that the FDIC will make scheduled payments of principal and interest on MCD through the mandatory conversion date.

Effective Date

Staff recommends that the Board find good cause for making this modification effective immediately as a final regulation.