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October 21, 2002

Robert E. Feldman
Executive Secretary
Attention: Comments/OES
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429

VIA EMAIL TO comments@FDIC.gov

Dear Mr. Feldman:

I am writing, as counsel to a number of community banks, to comment in support of the regulation proposed by the Federal Deposit Insurance Corporation ("FDIC") to be codified at 12 C.F.R. § 303.15 "Certain limited liability companies deemed incorporated under State law".

This letter will respond, in the order presented, to the FDIC's three questions raised in its request for comments in the Notice. 67 Fed. Reg. 48054 (2002) (to be codified at 12 C.F.R. Part 303) (proposed July 23, 2002).

Questions Presented.

1. Should the FDIC permit a State bank that is organized as an LLC to obtain Federal deposit insurance?

Comment. Yes, as long as the relevant bank chartering authority authorizes the structure as a bank charter. Organizers of banks should continue to have choices as they become available from bank chartering authorities, to select the type of charter a bank will have. Should the relevant chartering authority for national banks, state banks or thrifts authorize under applicable law or regulatory interpretation the issuance of a charter that is either an LLC or similar entity (e.g., the Limited Banking Association charter alternative for a Texas state bank under the Texas Finance Code and similar entities in Maine, Nevada and Vermont), the FDIC should entertain applications for insurance of accounts from such charters. If a chartering authority does not offer such an alternative, then, of course, a prerequisite for FDIC insurance is not met.

Similarly, existing insured financial institutions should be able to utilize available measures for converting to an LLC or similar charter.

Rationale. The choices available to organizers for forming an entity have increased and diversified. Businesses today can conduct operations as proprietorships, general partnerships and corporations, as they could under common law. Today's business organizers can also conduct operations in hybrid entities created under state laws, including, among others, limited partnerships, limited liability companies, limited liability, partnerships and close corporations, among others. Banks may not utilize a number of these entities, but if a chartering authority has concluded that a particular type of charter is suitable for a bank, the FDIC should certainly entertain an application for insurance of accounts for such bank and should permit other insured charters to retain insurance of accounts upon conversion to an LLC or similar charter.

2. If so, should the FDIC interpret the term "incorporated" utilizing some, all or none of "the traditional four corporate attributes"?

Comment. Not necessarily.

Rationale. According to the FDIC's statutory authority, the factors required to be considered by the FDIC in acting on applications for insurance of accounts are contained at 12 U.S.C. § 1816 as follows:

(1) The financial history and condition of the depository institution.

(2) The adequacy of the depository institution's capital structure.

(3) The future earnings prospects of the depository institution.

(4) The general character and fitness of the management of the depository institution.

(5) The risk presented by such depository institution to the Bank Insurance Fund or the Savings Association Insurance fund.

(6) The convenience and needs of the community to be served by such depository institution.

(7) Whether the depository institution's corporate powers are consistent with the purposes of this chapter.

No mention of any "four traditional corporate characteristics" is made in the statement of factors required for consideration by the FDIC. Even item (7), which uses the word "corporate" refers to powers and not "characteristics or features". In other words, it appears that item (7) refers only to powers derived from the entity's Articles of Association or applicable law. Furthermore, in practice, until the issue of limited liability entities as banks was raised by the FDIC, query if the FDIC has historically considered perpetual existence, limited liability, free transferability of interests and centralized management as factors necessary or even relevant to its overall review of insurance applications filed under 12 U.S.C. § 1815. If not, it seems inappropriate to require more of one charter than another, already insured charter.

Perpetual Existence

I know from experience that the FDIC has historically insured banks without perpetual existence. Until 1995, many such Texas state bank charters under the supervision of the Texas Department of Banking had limited periods of existence under their organizational documents and were nonetheless insured by the FDIC.

I do not disagree with the FDIC's statement in the Notice that it is charged with promoting the safety and soundness of banking institutions and with the duty of resolving failed institutions. But, I disagree that perpetual succession is a necessary ingredient in all charters to fulfill these roles as suggested in the notice. There are means available to obtain extensions of existence that have been used in the past with charters having limited existence. There is no reason why the FDIC should start requiring perpetual existence as a corporate attribute when it has not done so historically.

Free Transferability.

It also appears that the FDIC has not historically considered whether the stock of an institution was freely transferable in considering its application for insurance of accounts, because we have a number of bank clients that have both FDIC insurance and agreements restricting the transferability of the bank's stock.

I do not disagree with the FDIC's statement in the Notice that it is charged to consider the adequacy of a depository institution's capital structure and risk to the insurance fund under 12 U.S.C. § 1816. But with the number of insured closely held banks and other insured banks having restrictive shareholder agreements it would be inconsistent application of the FDIC's statutory authority to require free transferability of interest. A more measured approach could and should address the FDIC's concern. For example, the FDIC's policy statement on insurance of accounts states, regarding stock benefit plans, that they must contain a provision permitting the primary federal regulator to direct the plan participants to exercise or forfeit their stock rights if capital becomes inadequate. Similarly, the terms of an LLC bank's documents could be required to say that if capital is determined to be inadequate by the bank's primary regulator, then the current owners could be directed to replenish capital or waive the transferability restrictions. Accordingly, without unduly interfering in owners' rights, the FDIC could address its concern about capital adequacy.

Centralized Management.

We do not disagree that management of an institution is key to its success. It is undisputed that the FDIC is charged under 12 U.S.C. § 1816 to assess the "general character and fitness of management of the depository institution". Similarly, a chartering authority conducts reviews of management. For example, under the Texas Finance Code, the Texas Department of Banking is required to determine, among other things in order to grant a charter, that the banking experience, ability, standing, competence, trustworthiness and integrity of officers, directors (and their equivalent under the limited banking association structure) are sufficient to support the bank. Tex. Fin. Code Ann. § 32.003 (West 2002). This same review would be conducted if the bank were managed by a board of directors of a traditional bank or by members of an LLC bank through their human representatives.

Limited Liability.

It appears unnecessary to address whether limited liability is a factor significant to raising capital as stated by the FDIC since the LLC structure has limited liability as does a traditional charter and no distinction need be drawn on that factor.

3. If the FDIC should not utilize any of the four corporate attributes, how should it interpret the term "incorporated".

Comment. The FDIC should consider the term "chartered" to be synonymous with "incorporated" in this context.

Rationale. The FDIC should provide insurance in accordance with the terms of its statutory authority contained in the FDI Act.

In that regard, please note that the FDI Act does not require "four corporate characteristics" for any national bank or other bank eligible for insurance. Only a charter from a bank regulatory authority is required for a depository institution to be granted insurance of accounts.

The FDIC provides insurance of accounts pursuant to the Federal Deposit Insurance Act ("FDI Act") at 12 U.S.C. § 1815(a)(1), which provides in pertinent part, as follows:

> "...any depository institution which is engaged in the business of receiving deposits other than trust funds (as defined in section 3(p)), upon application to and examination by the Corporation and approval by the Board of Directors, may become an insured depository institution."

The FDI Act defines "depository institution" as "any bank or savings association". 12 U.S.C. 1813(a)

The term "bank" is defined, in pertinent part, as "any national bank, state bank,..."

The term "national bank" is not defined, but in practice, the FDIC insures deposits of national banks chartered pursuant to the National Bank Act. See *Interagency Charter and Federal Deposit Insurance Application*, OMB No. 3064-0001, page 1, stating the applicability of the form to, transactions among others, under the "National Bank Act, as amended (12 U.S.C. 21 *et seq.*), for a national bank charter".

Note also that directly following such item, the application states the applicability to *transactions* under "The state law for applying for state depository **charters**, as approved by state regulatory authorities" **[emphasis added]**.

If the FDIC intends to be consistent with published guidance, and internally consistent in its application of its deposit insurance granting authority to national and *state* chartered banks, interpretation of "incorporated" must mean "chartered", as reflected in OMB No. 3064-0001. To decide otherwise would impose requirements for obtaining FDIC insurance on state banks not present for national banks.

Summary.

State banks (or any other depository institution, for that matter) that meet the chartering authority's charter requirements should be permitted to submit applications to the FDIC for insurance of accounts. Existing insured depository institutions should be permitted to convert to an LLC charter or similar entity as permitted by the chartering authority and maintain their FDIC insurance. Any limitations imposed by the FDIC in exercising its statutory authority should be applied in a measured, not broad brush approach, only as necessary to fulfill its duties. The FDIC should exercise its statutory authority consistently with historical application. It is inconsistent with history to apply the "four factors" routinely and inconsistently with parity concepts to impose more onerous requirements on a state bank charter than upon a national charter in determining whether an entity should be granted FDIC insurance.

Thank you for this opportunity to comment.

Respectfully Submitted,

Carolyn V. Kelly

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