October 1, 2009

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

Re: Expiration of the Issuance Period for the Debt Guarantee Program; Establishment of Emergency Guarantee Facility

Dear Mr. Feldman,

We are students at the Morin Center for Banking and Finance Law at Boston University. We submit the following comments regarding the Federal Deposit Insurance Company's proposed alternatives for ending the Debt Guarantee Program (DGP). We would like to take this opportunity to express our support for the establishment of the Emergency Guarantee Facility (EGF) as embodied in Alternative B, as well as to articulate some of our concerns about the proposal in its current form.

I. The Case for Alternative B: A Smoother Transition Toward Self-Reliance

With the termination date of the DGP fast approaching, the establishment of an extended guarantee facility to offer further assistance to distressed institutions will provide a prudent and effective means of gradually phasing out what has proven to be a very successful strategy for stabilizing the liquidity and credit markets. As anxiety about the health of the banking system has recently eased, the number of entities utilizing the DGP has sharply decreased. According to data from Bloomberg, only $10.8 billion dollars in new FDIC-guaranteed bonds were issued in the third quarter of 2009, continuing a downward trend from $130.2 billion in the first quarter to $34.7 billion in the second quarter. Given the precipitous decline in the volume of banks that have sought FDIC assistance, it is unlikely that the proposed emergency plan will be overwhelmed by requests for guaranteed aid over the next several months. The conditions for participating in the proposed program are also sufficiently stringent as to deter all but the most necessitous institutions from applying. Applicants will be required to demonstrate their inability to issue non-guarantee debt due to market disruptions, and will have to receive approval from the FDIC chairperson after consulting with the board of directors in order to become eligible for the emergency window.

Nevertheless, because some institutions may still require additional backing, the proposed six-month extension will afford an appropriate period of additional time to verify the strength of the current recovery while providing the government with the flexibility to keep guarantee measures in place if the credit and liquidity markets were to seize up once again. Further disruptions are less likely to occur if financial institutions are able to retain the comfort of knowing that the guarantee option remains, rather than having to face the prospect of an abrupt and potentially premature cut-off of assistance. The

establishment of the EFG will therefore allow for a more orderly transition toward institutional self-reliance without inviting the risk of unwanted costs or abuse by undeserving institutions.

II. The FDIC should allow all financial institutions originally eligible under the DGP (not merely "participating institutions") that meet the criteria under Proposed Section 370.3(k) to participate in the EGF

By limiting the EGF to "participating institutions," the proposed regulation would exclude many distressed financial institutions in need of liquidity as a result of future market disruptions or other circumstances beyond the institution's control ("deserving nonparticipating institutions"[1]). While it is true the confidence and availability of credit in the market has increased substantially since the DGP was established, the effects of the current financial crisis are lasting and unpredictable. The shocks from the credit crisis may still be felt by participating and nonparticipating institutions alike; deserving nonparticipating institutions continue to be at risk of liquidity crises and failure.

As institutions continue to be at higher risk of failure, similar to the risks experienced by savings and loan associations through the late 1980s and early 1990s, widening the scope of the EGF to all institutions that would otherwise qualify under Proposed Section 370.3(k) would also (1) protect the Deposit Insurance Fund (DIP) and (2) perpetuate the main goals of the Temporary Liquidity Guarantee Program.

Regarding the former, the FDIC may help deserving nonparticipating institutions avoid receivership. Allowing nonparticipating institutions to participate in the EGF could help restore confidence and stability in these institutions by cloaking them with the aegis of guaranteed FDIC backing. Moreover, the FDIC should allow itself discretion to permit an entity to participate in a program that has resulted in a large monetary gain to the agency, rather than risk withdrawing even more funds from the diminishing reserves of the DIP. As to the latter, increased access to funds for troubled institutions will continue to aid in "preserving confidence in the banking system and encouraging liquidity in order to ease lending to creditworthy businesses and consumers."[2]

Finally, the costs to the FDIC from allowing nonparticipating institutions access to the EGF are likely to be relatively small. First, administrative costs are likely to increase minimally due to the probable paucity of new applications, considering: (A) the terms of the Emergency Guarantee Program are markedly more onerous than the previous DGP facility (e.g. executive compensation restrictions, substantially increased minimum assessments) and (B) fewer banks are using the current DGP.[3] Second, overall costs to the FDIC of the DGP, the use of which should reduce the likelihood of an institution's failure, are much less than the costs of receivership.

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[1] In other words, financial institutions that are able to demonstrate the inability to issue non-guaranteed debt to as a result of market disruptions or other circumstances beyond the entities' control.

[2] *See e.g.* 73 Fed. Reg. 72244 (Nov. 26, 2008).

[3] *See e.g.* 74 Fed. Reg. 47490 (Sept. 16, 2009).

III. The FDIC Should Retain the Discretion to Assess Annual Participation Fees below the Proposed level of 300 basis points

It is understood that the main goal of this proposition is to offer a time period extension for the program while limiting its accessibility to address only residual risks and emergency situations. As such, higher participation fees may provide an appropriate deterrent to applications motivated by other, less severe circumstances or concerns.

However, as mentioned above, data suggests that the TLGP and other federal efforts have had an effect to restore liquidity and confidence in the financial sector. Fewer participating entities are now issuing FDIC-guaranteed debt under the extended DGP, and a number of them conduct successful public offerings of non-FDIC-guaranteed debt and equity. Although the systemic risks seem to have diminished, the policy behind the creation of the existing program should be the same justifying its extension. Emergencies are unforeseeable and it may not be rational to enforce a one-way ratchet on yearly fees when the facts and circumstances of a particular institution's credit-worthiness and solvency are yet unknown. A minimal rate may be inconsistent with the very flexibility the program is seeking to provide. Therefore the FDIC should retain the discretion to either raise or lower the annualized assessment fees for participating institutions based on the risk that each institution's predicament presents, and not on the timing of their application.

IV. The Two-Pronged Challenge of Transparency

A. Transparency as a Requirement for the Predictability of the FDIC's Selection Criteria

As discussed above, we are encouraged by the FDIC stated goal of allowing the DGP to expire, and it is our belief that a phased withdrawal from this program is preferable to an abrupt exit. Still, we express concerns on the lack of predictability of the criteria required by the FDIC to make available to certain financial institutions its EGF.

Despite the detailed representations required by the FDIC from financial institutions wishing to be considered for the EGF (projections of the sources and uses of funds, summary of entity's contingency plans, description of plans for retirement of FDIC-guaranteed debt, etc.) what is lacking from the proposal are *clear guidelines and principles* as to what would constitute for the FDIC legitimate needs that would warrant its granting access to the EGF.

The FDIC describes its proposal as an emergency window "designed to address an entity's inability to replace maturing debt through non-guaranteed sources *as a result of a market disruption or other circumstance beyond the control of the participating entity*"(our emphasis). What is less clear are the kind of financial challenges that can reasonably be construed as stemming from market disruption, and conversely, which ones cannot. On a related note, although we acknowledge that the FDIC could not possibly list all the possible circumstances that could arise outside the direct control of a given entity, the overly broad language used by the FDIC to describe conditions that could warrant granting emergency relief to banks is problematic on at least two counts.

First, it hinders the efficacy of the program by making its bank's eligibility hard to predict. Second it reinforces a pervasive, yet commonly held belief (especially since the fall of Lehman Brothers last year), that the government can choose which bank can survive and which ought to fail based on its own subjective agenda.

B. Transparency as a Balancing Act: an Efficient Program vs. the Public's Right to Know

What remains unclear in the proposal is how disclosure requirements will be met during an entity's application for the EGF as well as how the outcome will - if at all - be disclosed and whether it would defeat the purpose of the program itself.

Considering the stringent conditions and the onerous financial burden assumed by entities applying for the program, it is fair to assume that the mere application of a financial institution for the FDIC's emergency window could be interpreted as a sign of great financial distress, which could in turn not defeat if not reverse some of the benefits of the program. In this context, would institutions be required to disclose their participation in the program? If so, what could help mitigate the aforementioned effects? If not, how would such financial institutions fulfill their disclosure requirements?

Perhaps more importantly, what is not clear under alternative B is whether or not financial institutions that have been denied the FDIC's EGF would have to disclose the fact that they applied and were denied such recourse. We argue that they should not because this disclosure requirement would in fact greatly hinder the program's efficacy by causing a "chilling effect" on any struggling institution. Indeed, any bank likely to seek the program's help would want to do so without jeopardizing its already fragile situation. If the FDIC's denial was to be burdened with a disclosure requirement, one wonders which bank, if any, would want to pursue such onerous and risky recourse.

Conclusion

As more and more financial firms regain the ability to issue debt without government backing, the interconnected relationship between government and the banking industry will continue to untangle. The establishment of the EGF holds great promise to further this end. However, it is crucial that the terms and conditions of participation in the facility offer an appropriate balance of incentives and restrictions to help the most vulnerable institutions find their footing without unduly prolonging the program or exacting counterproductive costs. We believe this balance can be more finely calibrated by adopting the following measures: 1) widening the field of participation to all institutions that would otherwise qualify under the criteria of Proposed Section 370.3k; 2) allowing greater discretion in assessing yearly participation fees; and 3) making participation criteria more transparent while taking steps to ensure that the denial of participation is kept in appropriate confidence.

Sincerely,

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