Joint Comment Letter

TRIUMPH | INVESTMENT | FUNDS

August 6, 2009

Mr. Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
Attention: Comments
550 17th Street, NW.
Washington, DC 20429

Re: Proposed Statement of Policy on
Qualifications for Failed Bank Acquisitions (RIN # 3064–AD47)

Dear Mr. Feldman:

Triumph Investment Funds and Nutter McClennen & Fish welcome the opportunity to comment on the FDIC's Proposed Statement of Policy on Qualifications for Failed Bank Acquisitions.[1]

Relevant Professional Experience

Triumph Investment Funds/Robert P. Keller

Triumph Investment Funds is a private equity firm based in Bedford, New Hampshire that invests in high performing community-based commercial banks, working with their management and boards to help them meet their capital needs for growth and profitability. Robert P. Keller, a Certified Public Accountant with over 30 years of experience as a senior bank executive and investor, has served as the co-head of Triumph Investment Funds since its inception in 2003. Triumph holds an equity position in approximately 35 community banks.

From October 1991 to June 1994, Mr. Keller served as President and Chief Executive Officer of New Dartmouth Bank, a privately-owned financial institution with assets of $1.7 billion, headquartered in Manchester, New Hampshire, which was acquired by Shawmut National Corporation in 1994. As discussed in greater detail below, New Dartmouth was organized specifically for the purpose of acquiring three failed banks from the FDIC in October 1991.

[1] 74 Fed. Reg. 32931 (2009).

From June 1995 to June 2001, Mr. Keller served as President and Chief Executive Officer of Eldorado Bancshares, Inc. ("ELBI"), a Nasdaq-listed bank holding company based in southern California with assets of $1.3 billion, which Zions Bancorp acquired in 2001. During his tenure at ELBI, Mr. Keller also served as the President and Chief Executive Officer of Dartmouth Capital Group, Inc., the general partner of Dartmouth Capital Group, L.P., a private equity fund that was a registered bank holding company and ELBI's largest shareholder. In 1997, ELBI raised approximately $70 million of acquisition financing from two private equity funds, Madison Dearborn Partners and Olympus Partners, each of which acquired a greater than 15 percent equity interest in ELBI.

Mr. Keller's other relevant professional experience includes 13 years as an officer of Indian Head Banks Inc. of New Hampshire; two years as the Executive Vice President and Chief Operating Officer of American Federal Bank in Dallas, Texas, which was created through the merger of 12 independent thrifts under the Southwest Plan; and one year as President and Chief Executive Officer of Independent Bancorp of Arizona, Inc., a Nasdaq-listed bank holding company with assets of $1.8 billion, which was acquired by Norwest Corporation in February 1995. Since September 2002, Mr. Keller has served as Chairman of the Board of Directors of Security Business Bank of San Diego, where he also serves as Chairman of the Director Compensation Committee and as a member of the Loan Committee.

Nutter McClennen & Fish/Michael K. Krebs

Nutter McClennen & Fish is a law firm with its principal office in Boston, Massachusetts. Nutter's banking and financial services attorneys represent a full range of financial institutions, including commercial banks, thrift institutions, trust companies, and bank and thrift holding companies, in regulatory, corporate, and litigation matters, as well as all legal aspects of their loan and investment transactions.

Michael K. Krebs is a partner at Nutter, where for over 20 years he has represented banking companies in mergers and acquisitions, securities offerings, and bank regulatory and corporate governance matters. Co-head of Nutter's Banking and Financial Services Practice Group, Mr. Krebs was counsel to New Dartmouth Bank in its transaction with the FDIC and its subsequent acquisition by Shawmut National Corporation. He also represented Dartmouth Capital Group, L.P. and ELBI from 1995 through 2001, and currently represents Triumph Investment Funds.

Executive Summary

The policy statement, if adopted as proposed, would impose significant burdens on bidders for failed banks that are backed by private equity investors and would likely squelch the interest those funds have in injecting new capital into the banking system to fund acquisitions of failed banks. These burdens would both be inconsistent with the FDIC's mandate to resolve failed banks at "the least possible cost to the deposit insurance fund"[2] and disregard the FDIC's positive experience with private equity-backed bidders during the last banking crisis.

Summarized below are our principal comments on the proposed policy statement. These comments address seven of the nine categories of questions on which the FDIC is explicitly seeking comments. In the following sections of this comment letter, titled "Fleet/KKR and New Dartmouth Experiences of the 1990s" and "Flaws in FDIC's Approach to Private Equity Investors under the Proposed Policy Statement," we discuss in more detail the historical basis and policy rationale for our comments.

What investors will be covered by the policy?

As proposed, the policy statement is directed at private equity investors that invest directly, or indirectly through a holding company, in a bank that assumes deposit liabilities, or both such liabilities and certain assets, from a failed insured depository institution in receivership (a failed bank).[3] One of the shortcomings of the proposed policy statement is that it fails to distinguish among the wide variety of private equity investors. On the one hand, a private equity investor may be a multi-million or even multi-billion dollar fund directed by professional managers that will acquire over 10 percent of the voting or equity interests of a bidder for a failed bank. On the other hand, a private equity investor may be an individual who meets the SEC's accredited investor test but will own less than 1 percent of a bidder for a failed bank.

The recent resolution of Security Bank Corporation of Macon, Georgia, illustrates the point. The FDIC approved a bid by an investor group led by Georgia banker Joe Evans in which the acquiring entity would be capitalized by $300 million raised from 26 investors—including, according to press reports, institutional investors and members of the new management team.

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[2] Federal Deposit Insurance Act § 13(c)(4)(B) (12 U.S.C. 1823(c)(4)(B)).

[3] *See* 74 Fed. Reg. 32931, 32933 (2009).

We submit that the focus of the proposed policy statement should be on private equity investors that have acquired within the past three years, or propose to acquire, a significant, though non-controlling equity stake, directly or indirectly, in a bank that acquires a failed bank, and that the policy statement should clarify the application of the policy through a more objective definition of the term "Investor." Specifically, we recommend that the policy statement define "Investor" to mean a beneficial owner, directly or indirectly, of 10 percent or more of the voting control or equity interests in a depository institution or holding company.

The Federal Reserve Board indicated in its recent Policy Statement on Equity Investments in Banks and Bank Holding Companies[4] that a minority investor generally would not have a controlling influence over a banking organization if the investor does not own or vote 15 percent or more of any class of voting securities of the organization, provided that the investor owns a combination of voting and nonvoting interests representing less than one-third in the aggregate of the total equity of the organization. If a private equity investor does not beneficially own, directly or indirectly, 10 percent or more of the voting control or equity interests in a depository institution or holding company, the investor clearly does not have a significant influence over the banking organization, and therefore such an investor should not be subject to the types of obligations and restrictions the FDIC proposes. Our proposed 10 percent threshold also is consistent with the federal regulations under the Change in Bank Control Act,[5] which in general establish a rebuttable presumption that an acquisition of voting securities of a bank or bank holding company constitutes the acquisition of control under the Change in Bank Control Act, requiring prior notice to the applicable federal regulator, if, immediately after the transaction, the acquiring person (or persons acting in concert) will own, control, or hold with power to vote 10 percent or more of any class of voting securities of the institution.

Following the convention of the proposed policy statement, we will refer to these private equity investors as "Investors."

What is the appropriate initial capital level?

A bank, which is backed directly or indirectly by Investors and acquires a failed bank, would be expected under the proposed policy statement to agree to maintain for at least three years a Tier 1 leverage ratio of not less than 15 percent, and *thereafter* continue to operate at a "well capitalized" level. If at any time the acquiring bank does not meet this standard, then the Investors would have to immediately facilitate restoring the institution to the "well

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[4] *See* Federal Reserve Board press release dated September 22, 2008, <www.federalreserve.gov/newsevents/press/bcreg/20080922c.htm>.

[5] 12 U.S.C. § 1817(j); *see, e.g.,* 12 C.F.R. §§ 303.80-86 and 12 C.F.R. §§ 225.11-17.

capitalized" level. Failure to maintain the required capital level would result in the acquiring bank being treated as "undercapitalized."[6]

We submit that the FDIC's proposed approach to capital ratios for banks capitalized by one or more Investors is flawed in three respects:

1. As explained in greater detail below, we believe that a prescribed minimum capital ratio would unwisely limit the FDIC's discretion.

2. If the FDIC chooses to prescribe a minimum capital ratio, or adopts presumption in favor of a minimum capital ratio, the minimum capital ratio should not be greater than the generally applicable threshold necessary to qualify as "adequately capitalized." On a case-by-case basis, the FDIC could impose a higher capital requirement on a bidder if the bidder's business or other circumstances warrant a higher capital ratio.

3. The FDIC should not have a separate and unequal capital scheme and Prompt Corrective Action regime for a bank that is backed directly or indirectly by Investors and acquires a failed bank. Similarly, the FDIC should not have the right to force the Investors to immediately facilitate restoring the institution to the prescribed capital level. Finally, the bank's failure to maintain the prescribed capital level should not result in the acquiring bank being treated as "undercapitalized" if the bank would not otherwise be considered undercapitalized under the Prompt Corrective Action regime.

Should the Source of Strength commitment be retained in the final policy statement?

Under the proposed policy statement, Investors' "organizational structures" would be expected to agree to serve as a "source of strength" for their subsidiary depository institutions, meaning the holding company through which the Investors have made their investments would be required to enter into an agreement to sell equity or engage in capital qualifying borrowing, if necessary, to support the subsidiary bank.[7]

The source of strength commitment should not be retained because it would introduce substantial uncertainty for Investors and would likely have a dramatic chilling effect on private equity investments in failed banks generally. The FDIC should not impose disparate treatment

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[6] *See id.*

[7] *See id.*

on the holding company through which the Investors make their investments in a bank that acquires a failed bank.

The Federal Reserve's source of strength doctrine requires that the capital of non-bank affiliates in a bank holding company structure be available as a source of support for the bank. Would the FDIC apply its source of strength commitment similarly, requiring a private equity investor that does not qualify as a bank holding company to risk their equity stakes in other non-bank affiliates to "engage in capital qualifying borrowing" to support the bank? Would the FDIC's source of strength commitments be consistent or even compatible with the Federal Reserve's source of strength doctrine for Investors that are bank holding companies? The uncertainty caused by imposing parallel and vague requirements alongside the Federal Reserve's existing, mature policy would likely deter private equity investments from institutional investors.

Should the Cross Guarantee commitment included in the Proposed Policy Statement be retained in the final policy statement?

When Investors in a holding company or bank that acquires a failed bank also hold investments, individually or collectively, that constitute a majority of the direct or indirect investments in one or more other FDIC insured banks, the proposed policy would require that Investors pledge to the FDIC their proportionate interests in each such bank to pay for any losses to the deposit insurance fund resulting from the failure of, or assistance provided to, any other such bank.[8] The cross guarantee is problematic in particular because it would likely reduce if not eliminate the prospect of an Investor participating in more than one "club deal" in which several private equity investors provide capital to support the acquisition of a failed bank's franchise, but none of the investors is deemed to be a holding company.

Is three years the correct period of time for limiting sales of the Investors' interest in the holding company or depository institution?

Under the proposed policy statement, an Investor in a holding company or bank that acquires a failed bank would be prohibited from selling or otherwise transferring securities of the Investor's holding company or bank for three-years absent the FDIC's prior approval.[9] We believe that the proposed holding period is arbitrary, ambiguous and, based on our experience, will likely chill the interest that private equity investors might otherwise have in providing capital to support the acquisition of one or more failed banks.

[8] *See id.*

[9] *See id.* at 32934.

The policy is arbitrary because the FDIC offered no support for three years as compared to a one- or two-year period. The policy is ambiguous because it is not clear how the policy would apply to a change in control resulting from a merger.

We recommend that the FDIC reduce the time period to not more than one year and clarify that the restriction would not apply in the event of a merger or other transaction that otherwise requires regulatory approval under the Bank Merger Act, the Change in Bank Control Act, the Bank Holding Company Act or the Home Owners' Loan Act.

Is the exclusion from bidding eligibility for Investors that, directly or indirectly, own 10 percent or more of the equity of a bank or thrift in receivership appropriate?

The proposed exclusion from bidding eligibility for Investors that, directly or indirectly, own 10 percent or more of the equity of a bank or thrift in receivership is inappropriate. The proposed exclusion presumes that each principal investor in a bank or thrift at the time it is placed in receivership is responsible for its failure. Such an assessment should be made only on a case-by-case basis.

Should the limitations in this Proposed Policy Statement be lifted after a certain number of years of successful operation of a bank or thrift holding company?

For the reasons outlined above and addressed in more detail below, we believe that the proposed policy statement should be modified so significantly that it may be more appropriate for the FDIC to abandon the initiative entirely. If, however, the FDIC decides to adopt the policy statement on substantially the terms proposed, then the generic limitations contemplated by the proposed policy statement, especially the enhanced capital requirements, should not last beyond three years. After that period, the FDIC should rely on the Uniform Financial Institutions Rating System, which is a more nuanced assessment of a banking organization's condition.

Fleet/KKR and New Dartmouth Experiences of the 1990s

There is nothing fundamentally novel about the current wave of bank failures or the desire of private equity investors to make opportunistic investments in banks that acquire the assets and liabilities of one or more failed banks. Toward the end of the last banking crisis in the late 1980s and early 1990s, many of the bank failures were concentrated in New England.[10] Perhaps the most memorable of these was the January 1991 closure of the Bank of New England and its two sister banks, Connecticut Bank & Trust Company and Maine National

[10] *See* Division of Research and Statistics, FDIC, *History of the Eighties — Lessons for the Future* 337 (1997).

Bank, with aggregate deposits of $19.1 billion.[11] The FDIC initially created three separate bridge banks, and on April 22, 1991, the FDIC Board of Directors approved a bid by Fleet Financial Group, Inc. (then known as Fleet/Norstar Financial Group, Inc.) for substantially all of the deposits and operations of the three bridge banks.[12]

The New England banking market continued to deteriorate following the Bank of New England takeover, with the epicenter of the banking crisis shifting north to New Hampshire by the latter part of 1991. According to an FDIC case study, the level of nonperforming assets in New Hampshire banks in 1991 was higher than it was for Texas banks in 1987, the peak year of nonperforming assets in that state.[13] In October 1991, the FDIC simultaneously resolved seven New Hampshire banks, including the five largest independently owned banks in New Hampshire, having total deposits of $4.4 billion. These deposits constituted 25 percent of all banking deposits in New Hampshire.[14] The deposits and certain assets of three of those failed banks were acquired by New Dartmouth Bank, which was organized specifically for that acquisition.[15] In total, New Dartmouth assumed $2.2 billion in deposits.

An essential ingredient that Fleet's acquisition of the Bank of New England franchise had in common with the New Dartmouth transaction was a significant capital infusion from private equity investors (and the FDIC). Fleet agreed to pay a $125 million premium to the FDIC and to raise $500 million of capital.[16] To finance the purchase, Fleet raised $708 million of which $283 million came from the private equity fund Kohlberg Kravis Roberts & Co. (KKR) and its investors, and $100 million came from the FDIC, which accepted Fleet preferred stock in exchange for a portion of the purchase premium.[17] KKR received convertible preferred stock and warrants to purchase shares of Fleet common stock. Together, this gave KKR the economic equivalent of a 16.5% equity stake in Fleet. Then FDIC Chairman Seidman said at the time, "We are delighted to see this new money coming into the banking system."[18]

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[11] *See* FDIC, *Managing the Crisis: The FDIC and RTC Experience* 635 (1998).

[12] *See id.* at 639-40.

[13] *See id.* at 667.

[14] *See id.*

[15] *See id.* at 674.

[16] *See* Doug Bailey and Peter G. Gosselin, *Fleet, Partner to Buy Bank of N.E. with $875M Offer*, Boston Globe, April 23, 1991, Business Section, at 1.

[17] *See Managing the Crisis*, *supra* note 11, at 641.

[18] FDIC News Release, PR-61-91.

New Dartmouth relied solely on private equity investors and the FDIC to provide the necessary capital to complete its transaction. New Dartmouth raised approximately $41 million of common equity from approximately 40 accredited investors, including individuals, private equity funds and pension plans. In addition, the FDIC invested $31 million in New Dartmouth in exchange for non-voting, non-cumulative perpetual preferred stock. The FDIC's investment was designed to be comparable to a private equity investment in a bank. The preferred stock, which qualified as Tier 1 capital, carried no cash dividend, but the redemption price increased by 7.2 percent each year until redeemed. In addition, the preferred stock, which was redeemable at any time, was convertible into common stock, initially on a 1-to-1 ratio after three years and increasing to a 1.25 to 1 ratio after the fifth anniversary. The structure of the preferred stock investment was designed to allow New Dartmouth to avoid paying dividends in its early years, while creating a strong economic incentive for New Dartmouth to redeem the FDIC's shares as soon as possible. Including the preferred equity and allowing for expected deposit run-off during the first six months, New Dartmouth had a *pro forma* Tier 1 leverage ratio of 4.0 percent when it opened in October 1991.

Flaws in FDIC's Approach to Private Equity Investors under the Proposed Policy Statement

The Fleet and New Dartmouth transactions demonstrate that significant private equity investment in a bidder for a failed bank is not incompatible with the FDIC's interest in efficient and cost-effective resolutions. These transactions also provide a prism through which we can consider how various aspects of the proposed policy statement would fundamentally alter the calculus for private equity investors who might otherwise be interested in providing capital to support the acquisition of one or more failed banks.

Enhanced Leverage Ratio Commitment

We can state with confidence that had the FDIC required New Dartmouth to maintain a Tier 1 leverage ratio of at least 15 percent for its first three years, New Dartmouth would have been unable to raise sufficient capital. Even with a very experienced and locally savvy management team and several well-regarded lead investors, New Dartmouth struggled to raise $41 million of common equity. Had the FDIC required an initial Tier 1 leverage ratio of 15 percent rather than 4 percent, the projected returns to common equity investors would have declined dramatically and the transaction could not have been financed.

We suspect the outcome would have been similar for the Fleet transaction. Even though, with the infusion of private equity from KKR, the FDIC and others, Fleet became one of the better capitalized banking companies of its size in New England, Fleet's *pro forma*

Tier 1 leverage ratio was only about 6 percent, not even half of the 15 percent ratio in the proposed policy statement.

The proposed policy statement notes that the "FDIC is also aware that new banks, regardless of their investor composition, pose an elevated risk to the deposit insurance fund since they generally lack a core base of business, a proven track record in the banking industry, and are vulnerable to significant losses in the early years of incorporation."[19] We believe the attempt to rationalize the requirement for a minimum 15 percent Tier 1 leverage ratio by analogizing to the typical experience of a start-up bank is disingenuous. Unlike a conventional start-up bank, which can be expected to lose money for the first two to three years while it establishes its deposit base, a winning bidder acquires from the FDIC a deposit franchise that typically has a substantial, seasoned depositor base that provides a lower cost foundation for the bank's funding needs and helps to boost the bank's profitability. In addition, the failed bank's franchise usually has mature operating systems and many experienced managers. Moreover, the loss sharing that the FDIC typically provides for the failed bank's problem loans purchased by the winning bidder further improves the risk profile for the bidder relative to a conventional start-up. New Dartmouth, for example, earned $15.5 million in approximately the first six months of operations for a return on average assets of 0.92 percent.

We believe that a prescribed minimum capital ratio would unwisely limit the FDIC's discretion. If, however, the FDIC chooses to prescribe a minimum capital ratio, or adopts presumption in favor of a minimum capital ratio, the minimum capital ratio should not be greater than the generally applicable threshold necessary to qualify as "adequately capitalized."[20] On a case-by-case basis the FDIC could impose a higher capital requirement on a bidder if the bidder's business plan or other circumstances warrant a higher capital ratio.

With respect to capital ratios applicable after the acquisition of a failed bank, the FDIC should not have a separate and unequal capital scheme and Prompt Corrective Action regime for a bank that is backed directly or indirectly by Investors and acquires a failed bank. Similarly, the FDIC should not have the right to force the Investors to immediately facilitate restoring the institution to the prescribed capital level. Finally, the bank's failure to maintain

[19] 74 Fed. Reg. 32931, 32933 (2009).

[20] Though we are encouraged by media reports of the FDIC's July 6, 2009 roundtable meeting regarding the proposed policy statement, suggesting that the FDIC is considering substantially reducing the minimum Tier 1 leverage ratio requirement to 8 percent, we believe that a fixed standard would unwisely limit the FDIC's discretion and that 8 percent is excessively high if the FDIC will not have the discretion to approve a lower capital ratio from time to time.

the prescribed capital level should not result in the acquiring bank being treated as "undercapitalized" if the bank would not otherwise be considered "undercapitalized."

According to the proposed policy statement, a bank that failed to maintain the prescribed capital level would be treated as ''undercapitalized'' for purposes of Prompt Corrective Action triggering various restrictions, including limitations on asset growth and capital distributions and capital restoration plan requirements. For example, one of the restrictions under the Federal Deposit Insurance Act is that an undercapitalized institution may not accept or renew brokered deposits.[21] It would be capricious to limit such a source of funding for a bank that is subject to the policy statement when it would otherwise be considered well-capitalized under the ordinary Prompt Corrective Action classifications. The enhanced capital ratio proposal also raises the question of when a bank that is subject to the policy statement might be classified as significantly or critically undercapitalized. If those thresholds are also above the measures used in the ordinary Prompt Corrective Action classifications, could the FDIC require extraordinary corrective action, such as ordering the institution to sell sufficient voting stock to reach the prescribed capital level, even if the institution would not be considered significantly undercapitalized under the thresholds used in the ordinary Prompt Corrective Action classifications?

The enhanced leverage ratio requirement in the proposed policy statement would overemphasize the Prompt Corrective Action regime to the detriment of the Uniform Financial Institutions Rating System, which is a more nuanced assessment of a banking organization's condition. The novel "undercapitalized" trigger the FDIC proposes may be contradictory to one or more components of the CAMELS rating on the organization, subjecting the organization to discriminatory sanctions as compared to similarly rated institutions that are not funded by private equity investments subject to the proposed policy statement.

Expanded Source of Strength Doctrine and Cross Guarantees

The proposed expanded source of strength doctrine and cross guarantee would breach the corporate wall between minority Investors and the entity, either holding company or bank, that acquires a failed bank. These provisions would introduce substantial uncertainty for Investors and would likely have a dramatic chilling effect on private equity investments in failed banks generally. In particular, the expanded cross guarantee would likely reduce if not eliminate the prospect of an Investor participating in more than one "club deal" in which several private equity investors provide capital to support the acquisition of a failed bank's franchise, but none of the investors is deemed to be a holding company. As the FDIC staff acknowledged in its supporting memorandum, club deals have played an important role in the

[21] *See* Federal Deposit Insurance Act § 29 (12 U.S.C. § 1831f).

resolution of two large banks during the current crisis.[22] In March 2009, the FDIC completed the sale of IndyMac to One West Bank, FSB, a newly formed federal savings bank, which was funded by a consortium of private equity investors that invested over $1 billion. Similarly, the FDIC sold BankUnited's operations in May 2009 to a newly chartered federal savings bank owned by a group of private equity investors, including W.L. Ross & Co. LLC, Carlyle Investment Management L.L.C., Blackstone Capital Partners V L.P., and Centerbridge Capital Partners, L.P., that invested $900 million. According to the FDIC, the respective bids of these investor groups were the least costly to the FDIC's Deposit Insurance Fund of all competing bids.[23] There is interest among private equity investors for many more club deals, but if the cross guarantee is not eliminated from the policy statement, the effect will be to discourage private equity investors from taking large, but non-controlling stakes, in more than one acquirer of a failed bank.

Three-year Holding Period

The proposed three-year moratorium that would restrict investors in a bank which acquires a failed bank's deposits from selling or otherwise transferring securities of the investors' holding company or depository institution, absent the FDIC's prior approval, is arbitrary, ambiguous and will likely chill the interest that private equity investors might otherwise have in providing capital to support the acquisition of one or more failed banks. The FDIC staff stated that the three-year moratorium is designed to ensure that investors are "committed to providing banking services to the community served by the acquired institution" and to provide a continued link with the parties with which the FDIC has entered into a loss sharing agreement.[24] This rationale is specious. The FDIC's statutory mandate is to resolve failed banks at "the least possible cost to the deposit insurance fund," not to paternalistically seek to ensure that particular investors – as opposed to the bank itself – are committed to providing banking services to the community served by the acquired institution.

As for the other consideration raised by the staff, if a creditworthy party assumes the acquirer's obligations under the loss sharing agreement, what more of a "link" to the parties to the loss sharing agreement does the FDIC need? Another important consideration is that it is not clear whether the three-year moratorium would apply to an acquisition of the acquirer through a merger.

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[22] *See* Memorandum from Sandra L. Thompson, Director, Division of Supervision and Consumer Protection and Michael Bradfield, General Counsel to the Board of Directors of the FDIC 2 (July 2, 2009) (<www.fdic.gov/news/board/jul2memo.pdf>).

[23] *See id.*

[24] *Id.* at 5.

The FDIC should be more interested in ensuring that a banking organization retains a qualified management team in the event of a transfer of ownership rather than concerning itself with continuity of the equityholders. To the extent that a transfer of an Investor's interest would involve a change in control, and therefore a possible change in management, the transaction would be subject to the application and approval requirements of the Change in Bank Control Act,[25] thus rendering the continuity of ownership restrictions superfluous.

Here again the New Dartmouth experience is instructive. In March 1993, not quite 18 months after its transaction with the FDIC, New Dartmouth agreed to be acquired by Shawmut National Corporation, a much larger regional banking company. This was an economically rational decision for both Shawmut and the New Dartmouth Board of Directors, which was comprised almost entirely of representatives of the private equity investors. Shawmut had overcome the challenges that it had confronted in the early 1990s and was interested in expanding into New Hampshire. The New Dartmouth franchise provided an attractive market extension for Shawmut. New Dartmouth's management had successfully integrated the three banking franchises it had acquired from the FDIC in October 1991, as well as a fourth smaller subsequent acquisition from the FDIC, and had established a track record of strong profitability. Moreover, New Dartmouth had already redeemed a substantial portion of the FDIC preferred stock, beginning in early 1993, and it had committed to redeem the balance prior to Shawmut's acquisition. There was no reason in 1993 why the FDIC or any other regulator should have treated the New Dartmouth/Shawmut transaction differently than any other similar proposed merger. The same logic holds true today.

Proposed exclusion of Investors that, directly or indirectly, own 10 percent or more of the equity of a bank or thrift in receivership

The proposed exclusion from bidding eligibility for Investors that, directly or indirectly, own 10 percent or more of the equity of a bank or thrift in receivership is inappropriate. The proposed exclusion presumes that each Investor in a bank or thrift at the time it is placed in receivership (or during the period leading up to a receivership) is responsible for its failure or had an obligation to fund a recapitalization but opted not to do so.

Such an assessment should be made only on a case-by-case basis. For example, an Investor may have provided equity capital in a good faith but ultimately ill-fated effort to saving a bank or thrift from failing. In another scenario, the Investor may have had a 10 percent or greater equity interest but may not have had board representation. Why penalize either investor? Conversely, there may be situations in which a holding company or a dominant shareholder or group of shareholders or their affiliates engaged in conduct as owners

[25] 12 U.S.C. § 1817(j).

or directors of the failed that calls into question whether they should be significant Investors in a bidder for such bank or thrift in receivership.

Simply stated, we are extremely skeptical that any Investor would look forward to receivership in the hope that the Investor would be able to benefit from loss sharing with the FDIC after the subsidiary bank or thrift is placed into receivership. In nearly all scenarios, an Investor would incur a total loss as a result of the receivership, and there would be no guarantee that the Investor would be able to acquire the failed bank or thrift from the FDIC.

Duration of proposed policy statement

For the reasons discussed above, we believe that it may be more appropriate for the FDIC to abandon the initiative entirely. If, however, the FDIC decides to adopt the policy statement on substantially the terms proposed, then the generic limitations contemplated by the proposed policy statement, especially the enhanced capital requirements, should not last beyond three years. After that period, the FDIC should rely on the Uniform Financial Institutions Rating System, which is a more nuanced assessment of a banking organization's condition.

In our experience, a banking company that completes a significant acquisition – including the acquisition of a failed bank or thrift from the FDIC as receiver – will have completed its integration and had sufficient time to validate its business plan within the first 12 to 24 months. The three-year period that we recommend will permit the bank or thrift's federal regulator to have completed at least two examinations. During those examinations, especially the second exam, the regulators will be able to assess whether the integration has been completed successfully and whether the business plan is viable. If as of the second examination there are significant doubts about the management, financial condition or prospects of the bank or thrift, the regulators should employ the usual supervisory devices (i.e., a board resolution, a memorandum of understanding or a cease and desist order) to more closely monitor and control the bank or thrift, rather than rely on the proposed policy statement.

Conclusion

As the Fleet/KKR and the New Dartmouth experiences demonstrate, several important aspects of the Proposed Statement of Policy on Qualifications for Failed Bank Acquisitions would create substantial disincentives for private equity investors to capitalize bidders for failed banks. The inevitable consequence of those disincentives is that there will be fewer bidders for failed banks, and in turn that reduction in competition will necessarily result in the FDIC receiving less economically attractive bids for failed banks, as illustrated by the reaction of Wilbur Ross, a prominent investor whose fund W.L. Ross & Co. participated in the Bank

United resolution. Mr. Ross is quoted as stating that if the policy statement had been in effect, he "would never have invested in Bank United."[26]

The bias against private equity investors evident throughout the proposed policy statement is directly at odds with the FDIC's mandate to resolve failed banks at "the least possible cost to the deposit insurance fund." It also disregards the FDIC's positive experience with private equity-backed bidders during the last banking crisis. For these reasons, we recommend that the FDIC substantially revise the policy statement consistent with the foregoing comments.

Again, we appreciate the opportunity to comment on the proposed policy statement. Please do not hesitate to contact us if you have questions about any view expressed in this letter.

Sincerely,

Robert P. Keller
Managing Director
Triumph Investment Funds
(603) 668-2301

Michael K. Krebs
Partner
Nutter McClennen & Fish LLP
(617) 439-2288

[26] Emily Flitter, *Investors, Regulators Rip Failed-Bank Plan*, American Banker, July 6, 2009, at 1.