DAVID L. LEDFORD

SENIOR VICE PRESIDENT
HOUSING FINANCE AND LAND DEVELOPMENT

August 7, 2009

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

Attention: Proposed Statement of Policy on Qualifications for Failed Bank Acquisitions
RIN 3064-AD47

Dear Mr. Feldman:

On behalf of more than 200,000 members of the National Association of Home Builders (NAHB), I am pleased to respond to the request for comments on the Federal Deposit Insurance Corporation's (FDIC's) *Proposed Statement of Policy on Qualifications for Failed Bank Acquisitions* (Proposal or SOP). The FDIC is seeking public input on the SOP which describes the terms and conditions that private capital investors would be expected to satisfy to obtain eligibility for a proposed acquisition of a failed insured depository institution. These measures would cover capital support, cross guarantees, transactions with affiliates and continuity of ownership requirements among other things.

Recently, an increasing number of private capital investors have indicated interest in purchasing insured depository institutions in receivership. In light of this and the growing number of bank and thrift failures, the FDIC has proposed policies for determining the appropriateness of a prospective acquisition of a failed banking institution by private equity investors. The FDIC is particularly concerned that owners of banks and thrifts, whether they are individuals, partnerships, limited liability companies or corporations, have the experience, competencies, and willingness to run the bank in a prudent manner, and accept the responsibility to support their banks when they face difficulties and protect them from insider transactions.

NAHB supports FDIC's efforts to protect the deposit insurance fund and ensure that investors of failed financial institutions have the necessary management skills and financial resources to provide support and essential safeguards to the acquired institutions. While NAHB agrees that non-traditional investors pose a higher degree of risk to the insurance fund, we are

concerned that the Proposed SOP could cut off this important source of capital to the banking system.

FDIC indicates that "substantial additional capital is needed in the US banking system…and it is keenly aware of this need, particularly as it arises in the context of its function as the receiver of failed insured depository institutions". The Proposed SOP, with its very restrictive provisions and undefined terminology, would drive away much of the very substantial amounts of investable funds held by private equity firms. In addition, it demonstrates a bias against private equity capital and appears to impose bank holding company like restrictions on non-controlling minority investors which would place unfair restrictions and requirements on private equity. The proposal would impose significant additional requirements and restrictions which run counter to the private equity model and could substantially reduce or eliminate this source of capital for failed banks.

The Federal Reserve published its own *Policy Statement on Equity Investments in Banks and Bank Holding Companies* in September 2008. The policy statement, in recognition of the financial crisis and the need for capital in the banking system, expanded rather than limited the ability of investors, including private equity firms, to acquire interests in insured institutions without being deemed to control the depository. The Fed recognized that minority investors in banking organizations typically seek to limit their potential downside financial exposure in the event of the failure of a banking organization. The Fed noted that "controlling influence determinations depend on the amount of influence the investor ***in fact*** exercises over the banking organization". Accordingly, the Board indicated the need to monitor carefully minority investments in banking organizations to ensure that investors do not exercise a controlling influence over the management or polices of the banking organizations in which they invest.

The Fed's Policy Statement reflects the reality of the market while ensuring that regulatory and supervisory tools will be used to ensure that minority investors, including private equity investors, do not exert undue influence over bank management, strategies and operations. In contrast, the FDIC's Proposed SOP appears to make the presumption that minority equity investors do influence bank management thereby necessitating the restrictive limitations and requirements enumerated in the Proposal.

Several provisions of the Proposed SOP would be particularly damaging to private equity investment:

1. **Capital Commitment:** The Proposed SOP requires a Tier 1 leverage ratio of 15 percent and this ratio must be maintained for a period of three years, and thereafter the capital of the insured depository institution must remain at a well capitalized level. Capital levels that fall below the standard for a well capitalized institution after the three year period will result in the institution becoming undercapitalized for purposes of Prompt Corrective Action triggering all of the measures that would be available to regulators in such a situation.

- The Tier I leverage ratio requirement under the Proposed SOP is three times higher than the current standard for well capitalized banks. In addition, de novo banks are subject to a much lower 8 percent Tier I leverage ratio for a three year period. The 15 percent leverage ratio will clearly make private equity investments in failed depositories uncompetitive and uneconomical and will potentially eliminate private equity as a source of capital altogether. In addition, there is the obvious question of fairness as standards for private equity will remain more restrictive than for more traditional ownership structures even if the institution is profitable and operated in a safe and sound manner.

2. **Source of Strength:** Investor organization structures, investing in a bank holding company, would be expected to agree to serve as a source of strength for their subsidiary depository institutions under a commitment to sell equity, engage in capital qualifying borrowing, or by other measures.

    - The term "investor organization structures" is not defined which raises numerous concerns. It does appear that the intent of the FDIC is to require minority equity investors to serve as a source of strength for the acquired institution. These uncertain stand-by obligations of private equity investors will reduce the flow of capital to the banking industry as it could dampen investor interest by requiring non-controlling investors to infuse additional funds into a troubled banking institution.

3. **Cross Guarantees:** Investors whose investments, individually or collectively, constitute a majority of the direct or indirect investments in more than one insured depository would be expected to pledge to the FDIC their proportionate interests in each such institution to pay for any losses to the deposit insurance fund resulting from a failed bank.

    - Under the cross-guarantee proposal, investors would pledge their proportionate interest in each institution to the FDIC to cover losses to the insurance fund from the failure of one of the institutions. It is not practical to enforce such a cross guarantee as doing so would pierce the limited liability that private investors seek, making investments in depository institutions undesirable.

4. **Transactions with Affiliates:** All extensions of credit to investors, their investment fund, any affiliates, and any portfolio companies (companies in which the investors or affiliates invest) by an insured depository acquired or controlled by such investors would be prohibited under the Proposal.

    - The restrictions that normally apply to a bank under Sections 23A and 23B of the Federal Reserve Act and various other Federal Reserve regulations are

replaced by an outright prohibition on covered transactions under the FDIC Proposal that would apply to all private equity investors and the funds that they control. Again, the Proposal appears to punish private equity capital, making bank acquisitions less attractive to this class of investors.

5. **Continuity of Ownership:** Investors subject to the SOP would be prohibited from selling or transferring securities of the holding company or depository institution for a three year period of time following acquisition.

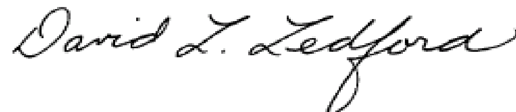
    - The holding period, while consistent with requirements for de novo institutions, would make investments in failed institutions less attractive to private equity firms who are accustomed to turning around substandard operations and seeking a profitable outcome when opportunities arise.

In closing, I appreciate this opportunity to comment on behalf of NAHB. It is laudable that the FDIC is addressing safety and soundness considerations when evaluating bids from private equity groups. The Proposed SOP however raises many concerns because of the significant new requirements and restrictions to be imposed on private equity investors in failed depository institutions. These roadblocks will discourage additional private equity investment in failed depositories at a time when more and more banks and thrifts are at risk of failure. NAHB urges the FDIC to modify or withdraw the Proposed SOP so that private equity investors are not encouraged to deploy their funds elsewhere. We also note that many of the FDIC's concerns, as outlined in the Proposal, can be addressed through the Bank Holding Company Act and through normal regulation and supervision.

Finally, it appears that the Proposed SOP would apply retroactively which would harm many private equity investors that have already executed purchase agreements with FDIC receiverships. NAHB urges the FDIC to develop prospective policies rather than making these rules retroactive.

Please direct questions regarding this matter to John Dimitri, NAHB's Director of Financial Institutions and Capital Markets, at 202-266-8529, or via e-mail at jdimitri@NAHB.com.

Sincerely,



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