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August 10, 2009

**Submitted Via Email**

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

**Re**: Proposed Statement of Policy for Failed Bank Acquisitions; RIN 3064–AD47; 74 Federal Register 32931

Dear Mr. Feldman:

The American Bankers Association (ABA) appreciates the opportunity to comment on the Proposed Policy Statement published by the Federal Deposit Insurance Corporation (FDIC). This Proposed Policy Statement would provide guidance to private capital investors interested in acquiring or investing in failed insured depository institutions regarding the terms and conditions for such acquisitions or investments (Proposed Policy Statement). Providing clear guidance to potential investors is critical to attracting fresh capital from a wide variety of sources to restore troubled banks to financial health and to minimize loss to the Deposit Insurance Fund (DIF). Given current market and accounting stresses on the banking industry, which have impacted even healthy banks (particularly those operating in economically distressed areas), acquisitions of troubled banks through banking industry mergers and acquisitions are limited. Therefore, it is important to recognize alternative sources of capital including, but not limited to, private investors.

We agree completely that all bank owners should have the experience, competence, and willingness to run the bank in a prudent manner and accept the responsibility to support their banks and protect them from inappropriate insider transactions. We further understand the FDIC's concern that in some cases new banks can pose an elevated risk to the DIF because they are vulnerable to loss in the early years of their existence. However, we respectfully submit that, in light of current statutes and regulations and the attention they give to relevant safety and soundness issues, the Proposed Policy Statement does not provide any additional necessary tools or standards, but it does contain elements that may actually be counterproductive to promoting the efficient resolution of failed institutions. Further, the Proposed Policy Statement does not explain why existing authorities are not sufficient. Indeed, the Proposed Policy Statement fails to explain why it is necessary to subject a particular class of investors to restrictions and scrutiny well beyond that which is

required of similarly situated investors under current statutes and regulations, and why such existing authorities are not sufficient to vet the applications of such class of investors. Accordingly, the ABA recommends that the FDIC refrain from finalizing the Proposed Policy Statement, in light of already established protections of insured depository institutions under the existing statutory and regulatory framework.

Our primary concerns may be summarized as follows:

- The current statutory and regulatory framework provides adequate authority for the relevant regulator to ensure that an investor group acts in a manner consistent with safety and soundness concerns.
- Many of the conditions that would be imposed under the Proposed Policy Statement would discourage potential investors from allocating capital to bank investments. (Indeed, we have already seen evidence of a chilling effect from the mere publication of the proposal.)
- However, we do agree with the imposition of a three-year minimum holding period for investments in failed institutions (unless otherwise agreed to by the FDIC), and we would support, on a case-by-case basis, a limitation on the ability of 10 percent investors to bid on the failed bank's assets.

These points are discussed in more detail below.

Importantly, we believe that the Proposed Policy Statement, if adopted as proposed, would deter significantly private equity investors, to the detriment of efficient resolution of failed depositories, the resources of the DIF, and the operation of the larger economy. Indeed, the release of the proposal is already discouraging private equity investors from moving forward on failed bank acquisitions. The Proposed Policy Statement could also have a chilling effect on non-private equity acquirers and investors that may be concerned about the application of similar restrictions through future regulatory action or as conditions to an acquisition or investment.

**Inappropriately restrictive standards.** We believe that many of the proposed standards would impose inordinately restrictive obligations on private equity investors that are not placed on other investors. These points are discussed in the following responses to the questions posed by the FDIC in the Proposed Policy Statement.

1. *The measures contained in the Proposed Policy Statement will not be applied to individuals, partnerships, limited liability companies, or corporations that accept the responsibilities under existing law to serve as responsible custodians of the public interest that is inherent in insured depository institutions, but will be applied to (a) private capital investors in certain companies, proposing to assume deposit liabilities, or both such liabilities and assets, from a failed insured depository institution in receivership (including all entities in such an ownership chain) and to (b) applicants for insurance in the case of de novo charters issued in connection with the resolution of failed insured depository institutions (hereinafter "Investors"). Is some other definition more appropriate?*

   We appreciate the FDIC's concern that acquirers of and investors in banks should appropriately disclose their ownership and operate in a manner that is transparent to the market and to regulators. We believe that the current statutory and regulatory framework provides for adequate and appropriate disclosure of ownership and business plans. If changes to the current framework are deemed necessary, they should be made through the legislative or regulatory process, as applicable.

Given our view that the Proposed Policy Statement is not needed, we advance no specific views on the definition of "investors." However, we would like to submit the following points in response to the FDIC's question. The Proposed Policy Statement contains an inherent presumption that private equity investors do not accept the responsibilities under existing law to serve as responsible custodians of the public interest. We believe this unfairly characterizes the private equity industry. Private equity investors are subject to extensive vetting under the statutory provisions applicable to changes in control of insured depository institutions. A prospective acquirer of a controlling interest in an insured depository institution must supply extensive information, including personal and business history, business background and experience, material business activities and affiliations, and any material pending legal or administrative proceedings. Financial information including a statement of assets and liabilities and related statements of income and sources and uses of funds prepared in accordance with Generally Accepted Accounting Principles must be filed. The prospective acquirer must identify the source and amount of funds or other consideration to be used in making the acquisition, any plans or proposals for major corporate changes to the institution, and any additional relevant information as the appropriate federal banking agency may require. Alternatively, a company (including a group acting in concert) may form a bank holding company, which process also requires the submission of extensive information regarding the identity and business dealings of the group and its members and requires an acceptance of the continued responsibilities and activity restrictions placed on bank holding companies. The extensive application process and continuing regulatory constructs to which prospective acquirers are subject under existing statute and regulation reach, in our view, the needs intended to be addressed by the Proposed Policy Statement and render the proposal at best redundant.

2. *The Proposed Policy Statement indicates that so-called "silo" structures would not be considered eligible bidders for failed bank assets and liabilities since under these structures beneficial ownership cannot be ascertained, the responsible parties for making decisions are not clearly identified, and/or ownership and control are separated. Are there any reasons why they should be considered to be eligible bidders?*

   Again, we understand the FDIC's concern about acquirers that are not fully transparent about their ownership and control structures. However, we do not believe an absolute prohibition on eligibility is necessary in order to advance the important interest in transparency. Under existing law and regulation, if an investor wishes to gain control of an insured depository institution, it must follow the procedures for a change in bank control or to form a bank holding company and furnish the required information. If an investor wishes to assume deposit liabilities of the bank, it is required to obtain approval of its application for deposit insurance. All such processes provide ample opportunity for regulators to question and ascertain the ownership and control structure of a bidder.

3. *One of the most important elements in the Proposed Policy Statement is the requirement that the acquired depository institution be very well capitalized. The text requires a tier 1 leverage ratio of 15 percent, that this ratio be maintained for a period of at least three years, and thereafter that the capital of the insured depository institution remain at a "well capitalized" level. The capital adequacy of depository institutions formed from assets and/or liabilities acquired from failed banks in receivership is a matter of crucial importance for reasons of safety and soundness and for protection of the Deposit Insurance Fund. … The FDIC seeks the views of commenters on the appropriate level of initial capital that will satisfy safety and soundness concerns*

*without making investments in the assets and liabilities of failed banks and thrifts uncompetitive and uneconomic.*

*Should there be a further requirement that if capital declines below the required capital level, the institution would be treated as "undercapitalized" for purposes of Prompt Corrective Action and the institution's regulator would have available all the measures that would be available in such a situation?*

We understand the FDIC's interest in ensuring that acquirers of failed banks operate with sufficient capital to minimize the risk that the bank will return to the category of troubled institutions. However, the proposal to impose a tier 1 leverage ratio of 15 percent for three years when the standard for other competitor banks would be significantly below that level would make many acquisitions and investments simply uneconomical. A tier 1 leverage ratio that is considerably higher than the regulatory minimum applied to other banks could also lead to unintended consequences by incenting excessive risk-taking. In order to achieve profitability and a return on equity comparable to their competitors, these banks could be under financial pressure to make riskier investments to compensate for the higher costs imposed by the regulatory capital surcharge. Alternatively, faced with the higher inherent cost of a bank acquisition, many potential bank investors may decide to pursue other business opportunities more likely to yield to their investment a competitive market return.

The proposed reclassification of the institution as "undercapitalized" for purposes of Prompt Corrective Action at levels far in excess of the standard applied to others in the industry would subject acquirers and investors to the risk of losing control of an institution that is being managed prudently and in a safe and sound condition. It is important to remember that under the prompt corrective action statute and regulations, an undercapitalized insured depository institution is subject to very severe restrictions. It must file a capital restoration plan and obtain supervisory approval to increase its assets or engage in acquisitions, branching, or any new business activities. It may not pay dividends or other capital distributions or make payments to certain persons in the form of management fees. The institution is subject to enhanced regulatory oversight by the appropriate federal banking agency. That agency may, in its sole discretion, take any additional actions it may deem appropriate including, but not limited to, requiring the owners of the insured depository institution to divest itself of the institution "if [it]… determines that divestiture would improve the institution's financial condition and future prospects." The agency can also take control of the insured depository institution by requiring, among other things, that it: (i) terminate or reduce certain activities or divest subsidiaries or affiliates; (ii) order a new election of directors; (iii) dismiss directors or senior executive officers and replace them with agency-approved personnel; and (iv) apply Section 23A of the Federal Reserve Act without regard to the exemptions thereunder. The scope of the agencies' authority over an institution that, under standards applying to the industry in general, would be well capitalized and in safe and sound condition, is extraordinary and excessive.

4. *Should the source of strength commitment included in the Proposed Policy Statement be retained in the final policy statement? Should the commitment be enhanced to require from the shell holding company and/or the Investors a broader obligation than only a commitment to raise additional equity or engage in capital qualifying borrowing?*

The source of strength doctrine should not be extended to ownership structures that are not bank holding companies under the Bank Holding Company Act. A bank holding company is expected to serve as a source of strength to its subsidiary depository institutions. The extension of this doctrine to investors that are not companies and are not acting in concert is not appropriate, as the investors may not possess a structure for common decision making and an individual investor may take actions not supported by the other investors. An investor should only be liable for its own actions and those taken by a company it has voluntarily elected to join. The extension of the source of strength doctrine to investors not acting in concert through a company would create a major disincentive to investments in failed banks.

5. *Should the cross-guarantee commitment included in the Proposed Policy Statement be retained in the final policy statement? Should the commitment contained in the Proposed Policy Statement be enhanced by requiring a direct obligation of the Investors?*

The Proposed Policy Statement would extend cross-guarantee liability to investors whose investments, individually or collectively, constitute a majority of the direct or indirect investments in more than one insured depository institution. This would impose an obligation on the owners of "chain" banking organizations to support each bank in the chain and would mitigate the impact on the DIF of recent failures of multiple banks under common ownership.

We understand the interests of the FDIC in holding significant investors to account for the losses of a bank when they presumably have the ability to prevent or mitigate these losses through shareholder action (e.g., by removing the chief executive officer). However, under the Proposed Policy Statement, a non-controlling investor in a failed bank could be subject to cross-guarantee liability if the collective investor "group" had a majority interest in the failed bank and then invested in other banks, even absent action in concert. An investor should only be liable for its own actions and those taken in concert with others through the formation of a bank holding company. If a policy statement is issued, it should clarify that a non-controlling investor would not be subject to a cross-guarantee.

Moreover, the FDIC has the ability to subject investors to cross-guarantee liabilities through making such liability a condition to the acquisition on a case-by-case basis. Therefore, the Proposed Policy Statement does not provide any necessary authority that the FDIC does not already possess, but it does potentially apply new requirements upon investor action that is not genuinely concerted action or interests.

6. *The Proposed Policy Statement limits the use of entities in an ownership structure that are domiciled in bank secrecy jurisdictions unless the investors are subsidiaries of companies that are subject to comprehensive consolidated supervision as recognized by the Federal Reserve Board. Should entities in bank secrecy jurisdictions be considered to be eligible bidders even without being subject to comprehensive consolidated supervision?*

We appreciate the FDIC's concern about the transparency of control of an insured depository institution. If an investor is seeking control of the insured depository institution, its jurisdiction of incorporation may become relevant to its ability to furnish to the appropriate federal banking agency(ies) the information required for the change in control or

bank holding company application. We would urge the FDIC to impose a more targeted review of potential investors from bank secrecy jurisdictions rather than a blind ban, and thereby to consider the adequacy and content of the actual information provided and available in either an acquisition or an investment.

If an investor is not seeking control of the failed insured depository institution but, rather, is seeking only to purchase certain assets or assume certain liabilities of the institution, the fact that it is domiciled in a particular jurisdiction should not alone be an impediment to its investment, neither should it prevent regulators from making appropriate inquiries in connection with relevant concerns. As noted above, the assumption of deposit liabilities is subject to an approved application for deposit insurance.

7. *Under the Proposed Policy Statement, Investors would be prohibited from selling or otherwise transferring securities of the Investors' holding company or depository institution for a three year period of time following the acquisition absent the FDIC's prior approval. Is three years the correct period of time for limited sales, or should the period be shorter or longer?*

A three-year retention period for the acquisition of control of an insured depository institution is reasonable to achieve a level of stabilization of a previously failed bank. We would, however, recommend that the FDIC retain the authority to waive the retention period requirement in appropriate cases.

Non-controlling acquisitions of securities by Investors should not trigger a three-year retention period. The responsibilities for providing financial support and managerial expertise assumed by a controlling investor are not the responsibilities of non-controlling investors. Thus, non-controlling investors should not be precluded from disposing of their investments at any time and FDIC approval should not be required for such dispositions. Imposing a retention period on non-controlling investors would simply incent them to invest in other markets where no such investment freeze requirements exist.

8. *The Proposed Policy Statement provides that Investors that directly or indirectly hold 10 percent or more of the equity of a bank or thrift in receivership would not be considered eligible to be a bidder to become an investor in the deposit liabilities, or both such liabilities and assets, of that failed depository institution. Is this exclusion from bidding eligibility appropriate on the basis of the need to assure fairness among all bidders and to avoid an incentive for the 10 percent or more Investor to seek to take advantage of the potential availability of loss sharing by the FDIC if the subsidiary bank or thrift enters into a receivership?*

We encourage the FDIC to consider this limitation on a case-by-case basis. A blanket limitation on the ability of a 10 percent investor to qualify as a bidder could deprive the FDIC of the ability to effect a least-cost resolution. Many investors have no direct role in the failure of a bank, but they may have a better understanding of the value of assets and deposits than would an investor with no connection to the bank.

We would, however, support limitations on the ability of an investor to bid on assets, such as loans or investments, in which it has an interest. This limitation should prevent an investor from improperly bidding to purchase its own loans at a deep discount.

9. *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? If so, what would be the appropriate timeframe for lifting the conditions? What other criteria should apply? Should all or only some of the conditions be lifted?*

   As noted in the introduction to this letter, we do not believe that the Proposed Policy Statement is necessary in light of existing law, regulation, and guidance. However, if the FDIC adopts a final policy, we would urge that the limitations contained therein be lifted no later than the third year of successful operation. This would coincide with the lifting of the ban on sales of controlling interests without the approval of the FDIC, as discussed in our response to Question 7.

**Other Comments**

*Transactions with Affiliates.* The restrictions of Sections 23A and 23B of the Federal Reserve Act present ample authorities to prevent self-dealing and conflicts of interest. The proposed absolute prohibition on extensions of credit to investors, their investment funds, and affiliates or portfolio companies of investors or their investment funds extends far beyond existing rules to prevent genuine conflicts of interest. It could deprive the insured depository institution of prudent and profitable lending opportunities and cause it to suffer competitive disadvantage.

Sections 23A and 23B of the Federal Reserve Act, and Regulation W thereunder, have had a long and successful track record of protecting banks from insider abuse. We see no compelling reason for imposing a different standard on acquirers of and investors in failed banks. Moreover, a complete ban on lending to acquirers and investors and their related interests would limit many prudent and profitable lending opportunities. Many acquirers and investors can bring business to an institution – both on the asset side through lending opportunities and on the liability side as a source of funding liquidity. Subject to the prudential requirements of the Federal Reserve Act and Regulation W, all insured depository institutions should be permitted to grow and profit from these business prospects.

*Disclosure.* The disclosure provisions of the Proposed Policy Statement extend far beyond what is necessary to ensure the fitness and propriety of investors in failed banks. The Proposed Policy Statement would require investors to submit extensive information that would likely include proprietary information; the proposal is silent on whether the FDIC would maintain the confidentiality of any proprietary information provided. Investors would have no means of ascertaining the scope of information that could be requested, as the Proposed Policy Statement would allow the FDIC to gather "such other information as is determined to be necessary to assure compliance with this policy statement."

The provisions relating to foreign investors are particularly troublesome, as they would require such investors to "consent to the disclosure of information that might be covered by confidentiality or privacy laws and to cooperate with the FDIC, if necessary, in obtaining information maintained by foreign government entities." This could place a foreign investor in the position of having to work with the FDIC to violate home country law in order to satisfy FDIC inquiries, an impossible condition that potentially could be reciprocally demanded of U.S. institutions operating abroad.

We understand the need for the FDIC to gather certain information about potential bank investors in order to determine the fitness and propriety of those persons. However, the overbroad disclosure

provisions of the Proposed Policy Statement would expose investors to intrusive scrutiny that would violate normal expectations of personal and corporate privacy and the protection of confidential and proprietary information. The disclosure provisions, if adopted as proposed, would deter private equity investors from engaging in failed bank acquisitions and investments and would disadvantage one class of investors vis-à-vis other investors.

*Cross Purposes with Current Economic Reality and Other Bank Regulators*. We also respectfully submit that the Proposed Policy Statement generally creates a regime of restrictions at odds with the importance – particularly in current economic conditions – of encouraging new capital investment in the banking industry, new capital that can have significant positive impact on economic recovery and the economic use of the resources of the DIF. Indeed, the Proposed Policy Statement runs counter to the efforts of other bank regulators to deal with the current economic, credit, and capital crisis. For example, the Federal Reserve in October 2008 published long-awaited additional guidance on control standards under the Bank Holding Company Act. It is our understanding that such guidance was released to make it clearer to private investors and non-bank holding company investors how to structure possible investments in and acquisitions of troubled banks and to facilitate increased investment. Further, the Office of the Comptroller of the Currency began providing guidance and approving so-called "shelf" charters for investors, thus purposely putting such investors and management teams through a thorough vetting process in advance so that they could more quickly come to the aid of troubled institutions in a bidding context. The Proposed Policy Statement in its likely effect stands in direct opposition to the efforts being made to increase capital and attract investors to the banking industry.

Thank you for considering our comments and recommendations. Please contact Mary Frances Monroe at (202) 663-5324 or at mmonroe@aba.com if you have any questions.

Sincerely,

Mary Frances Monroe