

Economic Crisis Response Group

Newsletter

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FDIC Adopts Final
Statement of Policy on the
Acquisition of Failed
Depository Institutions1

Federal Reserve Extends
TALF Program2

Bernanke Nominated for
Second Term as Federal
Reserve Chairman3

CFTC Comments on
Derivatives Legislation3

SEC and CFTC to Hold Joint
Meetings on the
Coordination of Derivatives
Regulation4

Treasury Department
Awards \$309 Million in
Grants to Develop
Affordable Housing Units4

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FDIC Adopts Final Statement of Policy on the Acquisition of Failed Depository Institutions

On August 26, the FDIC adopted a final Statement of Policy on the Acquisition of Failed Insured Depository Institutions (the “Policy Statement”), which provides guidance to investors seeking to acquire or invest in failed banks or thrifts about the criteria to qualify to participate in bids for such institutions. The Policy Statement amended a Proposed Statement of Policy on Qualifications for Failed Bank Acquisitions that the FDIC had published for comment on July 2 (the “Proposed Statement”).

The Policy Statement requirements include: (1) enhanced capital support of the acquired depository institution; (2) a cross-support obligation applicable to owners of 80 percent or more of commonly-owned depository institutions; (3) limits on transactions with affiliates; (4) requirements regarding continuity of ownership; (5) limits on investors from so-called “secrecy jurisdictions” that do not provide information with respect to potential money laundering; (6) limitations on special owner bids; and (7) more detailed disclosure requirements as to ownership and control.

Under the Policy Statement, holders of 10 percent or more of the equity of a failed bank are not permitted to bid for its assets. In addition, the Policy Statement prohibits the use of “silo structures” (structures used by private equity investors in which a separate investment vehicle is created to acquire financial institutions) in the acquisition of financial institutions.

The Policy Statement requires that acquired depository institutions be very well-capitalized (at a Tier 1 leverage ratio of 10 percent) for a period of at least three years, and at no less than a “well capitalized” level thereafter, and imposes a “cross-support” obligation on investors that own 80% or more of two or more banks or thrifts. These requirements are less stringent than the provisions contained in the Proposed Statement. The Proposed Statement required a Tier 1 leverage ratio of 15 percent and imposed a “source of strength” principle on investors (*i.e.*, investors’ organizational structures would be expected to support the depository institutions) as well as cross-guaranty obligations (such that controlling owners of multiple depository institutions would be expected to pledge to the FDIC their proportionate interests in each institution to pay for any losses incurred by the FDIC in liquidating or assisting any affiliated institution).

The Policy Statement applies to private investors in a company, including a company acquired to facilitate bidding on failed depository institutions, and applicants for insurance in the case of de novo charters issued in connection with the resolution of depository institutions, but does not apply to (1) certain investors in partnerships with bank or thrift holding companies that have a majority interest in the resulting bank or thrift and an established record for successful operation of insured institutions or (2) investors with five percent or less of the total voting power of the acquired institution.

The FDIC's position seeks to balance the need to tap alternative sources of capital to shore up failing banks with a concern that the interests of private equity investors (including risk calculus, affiliate transactions and exit strategy) may impact regulatory notions of prudence and continuity. The extent to which the FDIC position will brake private equity interest in bank investments remain to be tested.

Federal Reserve Extends TALF Program

On August 17, the Federal Reserve and the Treasury Department announced an extension of the Term Asset-Backed Securities Loan Facility ("TALF"), which had been set to expire on December 31, 2009, through June 2010. TALF is designed to increase credit availability and support economic activity by facilitating renewed issuance of consumer and business asset-backed securities ("ABS") at interest rate spreads closer to the range of historical experience.

The Federal Reserve and the Treasury noted that although conditions in financial markets have recently improved, securitization markets are still impaired and are expected to remain so for some time. Accordingly, the Federal Reserve and the Treasury have extended TALF loans against newly issued ABS backed by consumer and business loans and for legacy commercial mortgage-backed securities ("CMBS") through March 31, 2010. TALF loans against newly issued CMBS have been extended through June 30, 2010, reflecting the fact that these deals typically take longer to arrange. In addition, the Federal Reserve and the Treasury, citing market conditions, announced their decision to hold in abeyance the expansion of types of collateral eligible for the TALF.

The Federal Reserve stated that it will continue to monitor financial conditions to determine whether further extension or expansion of the program is warranted.

Bernanke Nominated for Second Term as Federal Reserve Chairman

On August 25, President Obama announced his decision to nominate Ben Bernanke for a second term as Federal Reserve Chairman. The announcement was widely interpreted as a signal of continuity in U.S. economic policy implemented in response to the crisis in financial markets that began in 2008. Under Mr. Bernanke's leadership, the Federal Reserve responded to the collapse of global credit markets by reducing interest rates to near zero, implementing programs to add liquidity to credit markets, and providing direct loans to large financial institutions whose failure posed a systemic risk to financial markets; these measures are generally credited with bringing a degree of stability to financial markets.

In his second term, Chairman Bernanke is expected to implement the Federal Reserve's exit strategy from these programs. In particular, Chairman Bernanke and the Federal Reserve will need to determine how quickly to wind down the various liquidity programs and to increase short-term interest rates.

Chairman Bernanke's reappointment is subject to confirmation by the U.S. Senate.

CFTC Comments on Derivatives Legislation

On August 11, CFTC Chairman Gary Gensler indicated his support of the Treasury Department's proposal to regulate OTC derivatives, but stated that the proposal would need to cover all derivatives with no exceptions. On August 19, he sent certain members of Congress a number of suggested revisions to the proposed legislation that would make the proposed regulation more stringent and comprehensive, eliminating certain exceptions to regulation.

Chairman Gensler's proposed changes would (1) narrow or eliminate mandatory clearing and trading exceptions for swap parties that are not dealers or "major swap participants" and foreign-exchange ("F/X") swaps exemptions; (2) eliminate dual regulation by the SEC and CFTC, with sole regulation by the agency with primary jurisdiction; (3) expand anti-fraud coverage for F/X swaps; and (4) repeal portions of the Federal Deposit Insurance Corporation Investment Act of 1991 so that financial institutions would be required to register with the CFTC or SEC in order to trade in OTC derivatives. Chairman Gensler also has asked Congress for a large increase in the CFTC's budget, since various proposed legislation would expand the CFTC's jurisdiction over derivatives.

SEC and CFTC to Hold Joint Meetings on the Coordination of Derivatives Regulation

The Securities and Exchange Commission (“SEC”) and the Commodity Futures Trading Commission (“CFTC”) plan to hold joint meetings on September 2 and 3 for public comment by market experts and participants on coordinating the regulation of over-the-counter (“OTC”) derivatives. CFTC Chairman Gary Gensler and SEC Chairman Mary Schapiro each made statements supporting the harmonization of their agencies’ approaches to regulating OTC derivatives.

The proposed coordination would eliminate gaps in areas where neither agency regulates, eliminate overlaps in regulation, and promote consistency and communication between the agencies.

Treasury Department Awards \$309 Million in Grants to Develop Affordable Housing Units

On August 26, the Treasury Department announced that \$309 million in grants under the American Recovery and Reinvestment Act (“Recovery Act”) had been awarded to communities in Arizona, Connecticut, North Carolina, North Dakota, Pennsylvania, South Carolina and Vermont to spur the development of affordable housing units. The funds are part of a Treasury Department program that will award more than \$3 billion under the Recovery Act to state housing agencies to create jobs and build affordable housing for individuals and families affected by the current economic crisis.

Proskauer's Economic Crisis Response Group includes lawyers with extensive experience representing private and public companies, institutional investors, financial services companies, private equity and hedge funds, lenders, commercial banks and individuals in the complex and interrelated areas impacted by the current financial situation. Our multidisciplinary group brings together the talents of our business and transactional lawyers with our litigation capabilities, particularly as they pertain to acquiring, managing or disposing of distressed assets; issues concerning investments in financial services companies; and complex financial instruments and transactions, including structured finance products; as well as a broad range of other areas such as corporate governance and defense, insurance coverage, reductions in force and other employment and benefit-related issues, securities regulation, and bankruptcy and restructuring matters.

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This publication is a service to our clients and friends. It is designed only to give general information on the developments actually covered. It is not intended to be a comprehensive summary of recent developments in the law, treat exhaustively the subjects covered, provide legal advice, or render a legal opinion.

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