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Insolvencies of "Systemically Significant Financial Companies" (SSFCs): Proposal for Federal Deposit Insurance Corporation (FDIC) Resolution

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Summary

This report briefly describes the draft of legislation issued by the Department of the Treasury on March 25, 2009, to provide the federal government with authority to resolve insolvencies of "systemically significant financial companies" (SSFCs). Although there is in place a means by which the federal government may oversee an orderly winding down of a bank which is insolvent or in danger of default, there is no such mechanism other than bankruptcy court for a securities firm, such as Lehman Brothers, or a mega insurance company, such as American Insurance Group (AIG), which is supervised as a thrift holding company. To remedy this situation, the draft language would provide the federal government with authority to resolve insolvencies of SSFCs—bank, financial, or thrift holding companies; insurance companies; and securities firms, identified as SSFCs on the basis of their size; extent of dealings; credit exposure; importance as a credit source for consumers, businesses and governments; and role in providing liquidity for the financial system.

The current legal situation leaves no alternative but bankruptcy court for all of these firms. Although current law provides for federal conservatorship and receivership of banks and thrifts and certain government-sponsored enterprises, the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac), and the Federal Home Loan Banks (FHLBs), the only current law means of handling an insolvency is bankruptcy court. The holding companies are not covered by the provisions of federal law delegating authority to the Federal Deposit Insurance Corporation (FDIC) to act as receiver or conservator of failed insured depository institutions. Insurance company insolvencies may be handled under state law.

Treasury's proposal is modeled on the authorities given to the FDIC. It includes broad powers to intervene in the face of insolvency and wind down, operate, merge, or otherwise deal with an insolvent SSFC and its assets and creditors—including creating a bridge financial institution. The proposal is likely to be followed by further draft legislation calling for the establishment of a new regulator to oversee the operations of SSFCs and the realignment of the federal regulation of the financial services industry.

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Background

On March 25, 2009, the Department of the Treasury issued draft legislative language[1] embodying a proposal to provide the federal government with authority to resolve insolvencies of "systemically significant financial companies" (SSFCs). Currently there is no such mechanism other than bankruptcy court for a bank, thrift, or financial holding company, such as Citigroup, a securities firm, such as Lehman Brothers, or a thrift holding company, such as the mega insurance company, AIG.[2] To remedy this situation, the draft language would provide the federal government with authority to resolve insolvencies of SSFCs—bank, financial, or thrift holding companies; insurance companies; and securities firms, identified as SSFCs on the basis of their size; extent of dealings; credit exposure; importance as a credit source for consumers, businesses and governments; and role in providing liquidity for the financial system.[3]

Current law leaves no alternative but bankruptcy court for these types of firms. The U.S. Code[4] authorizes federal conservatorship and receivership of banks and thrifts[5] and certain government-sponsored enterprises—the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac), and the Federal Home Loan Banks (FHLBs). For other financial firms, bankruptcy court is the only means of handling an insolvency.

Companies owning a bank or a thrift (i.e., bank holding companies, financial holding companies, and thrift or savings and loan holding companies), which are subject to "umbrella federal regulation" by the Board of Governors of the Federal Reserve System (Fed) or the Office of Thrift Supervision (OTS), are not treated as banks and thrifts for purposes of the authority of the Federal Deposit Insurance Company (FDIC) to act as receiver or conservator of failed insured depository institutions. They are subject to the federal bankruptcy code. Insurance company insolvencies are handled under state law. AIG, which is a mega insurance company with multiple subsidiaries and international operations, would be subject to bankruptcy court although it is a thrift holding company by virtue of owning a thrift.[6] So, too, would securities firms, hedge funds, commodities and futures trading firms.

Treasury's proposal is modeled on the authorities given to the FDIC. It includes broad powers to intervene in the face of insolvency and wind down, operate, merge, or otherwise deal with an insolvent SSFC and its assets and creditors—including creating a bridge financial institution. It

[1] The proposal is to be known as the "Resolution Authority for Systemically Significant Financial Companies Act of 2009) (hereinafter, Treasury's March 25, 2009 proposal). Text can be found at http://www.ustreas.gov/press/releases/reports/032509%20legislation.pdf.

[2] Since May 15, 2000, AIG has controlled AIG Federal Savings Bank (FDIC Certificate No. 35267) and is, therefore, a thrift or savings and loan holding company (Holding Co. No. H2984), regulated by the OTS. [http://www.ots.treas.gov/?p=InstitutionSearch&hid=H2984].

[3] Hedge funds operate similarly to mutual funds, pooling capital raised from investors and using it to buy and sell securities and other forms of investment vehicles or assets. They are structured to avoid Securities and Exchange Commission regulation either as issuers of securities or mutual funds by setting a minimum investment limit in the millions. Many are structured as limited partnerships and offshore, e.g., in the Cayman Islands. For further information *see* CRS Report 94-511, *Hedge Funds: Should They Be Regulated?*, by Mark Jickling.

[4] *See* CRS Report RL34657, *Financial Institution Insolvency: Federal Authority over Fannie Mae, Freddie Mac, and Depository Institutions*, by David H. Carpenter and M. Maureen Murphy.

[5] Under certain conditions, the National Credit Union Administration may act as conservator,12 U.S.C. § 1786(h), or liquidating agent, 12 U.S.C. § 1787, of a failed federal or federally-insured credit union.

[6] The thrift which AIG owns or controls would not be included in the bankruptcy court proceedings.

places the resolution authority for a SSFC with the FDIC. The proposal is likely to be followed by further draft legislation calling for the establishment of a new regulator to oversee the operations of SSFCs and the realignment of the federal regulation of the financial services industry.

Treasury's March 25, 2009, Proposal

What Types of Companies Does It Cover?

The March 25, 2009, Treasury proposal covers "financial companies," which it defines to include: (1) bank holding companies (BHCs)[7]; (2) financial holding companies (FHCs)[8]; (3) savings and loan holding companies (S&LHCs)[9]; (4) holding companies of insurance companies[10]; (5)

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[7] Under the Bank Holding Company Act (BHCA), 12 U.S.C. § 1841(a), a bank holding company (BHC) is any company that controls a U.S. bank, i.e., a bank chartered by state or federal government to do banking in the United States (as distinguished from a foreign bank—a bank chartered by a foreign government and doing business in the United States pursuant to the terms of the International Banking Act of 1978, 12 U.S.C. §§ 3101-3111). A foreign bank may also control a bank chartered in the United States and, thus, would be regulated as a BHC with respect to that U.S. bank. Under the BHCA, the activities of BHCs are generally restricted to banking, managing banks, and activities which the Board of Governors of the Federal Reserve System (FRB) had determined, prior to the enactment of the Gramm-Leach-Bliley Act (GLBA), on November 12, 1999, to be "so closely related to banking as to be a proper incident thereto." 12 U.S.C. §§ 1843(c)(1) and (c)(8). Appendix B to this report contains the statutory list of non-banking activities; Appendix C, the FRB's regulation, expands upon this list.

[8] Under the BHCA, as amended by GLBA, financial holding companies (FHCs) are BHCs which are authorized to engage in activities beyond those which are authorized for bank holding companies. 12 U.S.C. §§ 1841(l) and 1843(l). There is a list of financial holding companies on the FRB website at http://www.federalreserve.gov/generalinfo/fhc/. As of March 27, 2009, that list included 810 financial holding companies. The types of expanded financial activities authorized for FHCs are: any activity that the FRB has determined to be "financial in nature or incidental to such financial activity" or "complementary to a financial activity and does not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally." 12 U.S.C § 1843(k)(1). There is a statutory list of activities considered "financial in nature." 12 U.S.C. § 1843(k)(4). It includes lending; insuring; providing financial, investment, and economic advisory services; and underwriting securities. Appendix D contains the FRB regulation listing activities that are "financial in nature" or "complementary to a financial activity.... "

[9] Under the Savings and Loan Holding Company Act (S&LHCA), 12 U.S.C. § 1467a, a savings and loan holding company (S&LHC) is a company which controls a savings association (or thrift) and is, thereby, subject to the registration, examination, supervision, and activities restrictions of the S&LHCA as administered by OTS. The activities restrictions do not apply to certain grandfathered unitary thrift holding companies, i.e., S&LHCs controlling one savings association provided that the company is not sold and that the savings association maintains a specified percentage of its assets invested in residential mortgages and, thereby, meets the quality thrift lending test. 12 U.S.C. §§ 1467a(c)(3) and (m). Unitary thrift holding companies may engage in a full range of commercial activities. Among the unitary thrift holding companies are: General Electric Company (S&LHC No. H3028); General Electric Capital Corporation (S&LHC No. H3759); and General Electric Capital Services, Inc. (S&LHC No. H3758). They control one thrift, GE Money Bank (FDIC Certificate No. 27134). They also own another FDIC-insured institution, GE Capital Financial Co. (FDIC Certificate No. 33778). Since GE Capital Financial Co. is an industrial loan company, GE's ownership of it does not place it under the restrictions of the BHCA. *See* CRS Report RL32767, *Industrial Loan Companies/Banks and the Separation of Banking and Commerce: Legislative and Regulatory Perspectives*, by N. Eric Weiss.

[10] Unlike, BHCs, S&LHCs, and FHCs, for which there are federal law definitions, there appears to be no definition in federal law for insurance company holding companies. The OTS *Holding Company Handbook* contains a section on Insurance Holding Companies, which covers OTS supervision of S&LHCs in which there is an insurance subsidiary. That section of the manual is available on the OTS website at http://files.ots.treas.gov/4210018.pdf. Insolvencies of insurance companies, as distinguished from their holding companies, are administered in state courts and, in many cases, under an insolvency regime based on the National Association of Insurance Commissioners' Rehabilitation and Liquidation Model Act. Bankruptcy court is available for insolvencies of holding companies of insurance companies. This raises the possibility of jurisdictional conflicts when both are insolvent and the assets are one is held by the other (continued...)

holding companies of a broker or dealer;[11] (5) a holding company of a futures commission merchant or a commodity pool operator;[12]and (6) and a subsidiary[13] of any of the companies described in (1) to (5) except depository institutions and their subsidiaries,[14] brokers or dealers registered with the SEC and belonging to the Securities Investor Protection Corporation,[15] or insurance companies.[16]

What Is a Systemic Risk Determination?

Under the proposal, a systemic risk determination has three ingredients: (1) there must be a finding that "a financial company is in danger of default"; (2) that finding must be accompanied by a conclusion that its failure and resolution under otherwise applicable federal or state law "would have serious adverse effects on financial stability or economic conditions in the United States"; and (3) a determination that any actions or assistance as authorized in this proposal "would avoid or mitigate such adverse effects."[17]

(...continued)

at the time bankruptcy is filed or the receivership declared. *See* William Goddard, "In Between the Trenches: The Jurisdictional Conflict Between a Bankruptcy Court and a State Insurance Receivership Court," 9 Conn. Ins. L. J. 567 (2003).

[11] Although there appears to be no federal statutory definition of this type of company, the term appears to include companies, other than financial holding companies, which have broker-dealer subsidiaries, e.g., Pacific Select Group, LLC, [http://www.pacificlife.com/Channel/News/Current+Press+Releases/Pacific+Life+Forms+New+Holding+Company+For+Its+Retail+Broker+Dealer+Subsidiary.htm.] The term, thus, would apply to companies which have as subsidiaries, brokers or dealers registered with the Securities Exchange Commission under the Securities Exchange Act of 1934, 15 U.S.C. § 78o(b).

[12] Although there appears to be no federal statutory definition of this type of company, the term appears to include companies, other than financial holding companies, which have futures commission merchants and commodity pool operators as subsidiaries. Under the Commodities Exchange Act, futures commission merchants and commodity pool operators must register with the Commodities Futures Trading Commission, 7 U.S.C. §§ 1- 27f.

[13] As of May 5, 2003, Citigroup, a financial holding company, had "more than 1,900 subsidiaries throughout the world actively engaged" "in a broad range of financial activities, including lending, leasing, insurance underwriting and brokerage, securities underwriting and dealing, trust, investment advisory and data processing activities." Letter from Carl V. Howard, General Counsel—Bank Regulatory, Citigroup, Inc., to the Federal Trade Commission, Re: Telemarketing Rulemaking, at 3 (May 5, 2003). Citigroup's "Family Tree" shows the Citigroup's growth and provides an overview of its organizational chart. http://www.citigroup.com/citi/corporate/history/data/tree85x11.pdf. Other versions of this chart are available at http://www.citigroup.com/citi/corporate/history.

[14] Depository institutions and their subsidiaries are subject to the FDIC's conservatorship-receivership authority. *See* CRS Report RL34657, *Financial Institution Insolvency: Federal Authority Over Fannie Mae, Freddie Mac, and Depository Institutions*, by David H. Carpenter and M. Maureen Murphy.

[15] The Securities Investor Protection Corporation (SIPC), established under the Securities Investor Protection Act, 15 U.S.C. §78aaa et *seq.*, SIPC is a nonprofit, membership corporation, funded by its member securities broker-dealers. When a broker-dealer fails, SIPC will restore missing cash, stocks and bonds to customers from the assets of the insolvent firm; it will use its funds up to $500,000 per customer. With large firms, SIPC will seek to have a court-appointed trustee liquidate the firm and restores missing securities to customer accounts. It does not cover: commodity futures contracts, currency contracts, or investment contracts (such as limited partnerships) that are not registered with the SEC under the 1933 Securities and Exchange Act. For further information, *see* SIPC website at http://www.sipc.org/.

[16] Under the McCarran-Fergusson Act, 15 U.S.C. §§ 1511, *et seq.,* the regulation of insurance is a matter of state law. Insurance companies are covered by an exception to the Bankruptcy Code. 11 U.S.C. § 109(b)(2). Resolution of an insurance company's insolvency or threatened insolvency is a matter for a receivership in the court of the state in which the insurance company is domiciled; the holding company's bankruptcy or insolvency must be handled in federal bankruptcy court.

[17] Treasury's March 25, 2009, proposal, §§ 2(b)(2)(A)-(C).

What Is "Default or Danger of Default"?

For the Secretary of the Treasury to make the Systemic Risk Determination, the company must be in "default or danger of default." The proposal lists five standards for establishing that a company is in "default or danger of default." These are similar, but less extensive than those permitting an FDIC receivership or conservatorship of an insured depository institution.[18] The conditions are:

- The company is in bankruptcy court or a bankruptcy case "likely will promptly be commenced."[19]
- The company is critically undercapitalized.[20]
- The company "has incurred, or is likely to incur, losses that will deplete all or substantially all of its capital, and there is no reasonable prospect for the company to avoid such depletion without assistance" that FDIC may provide under the terms of this proposal.[21]
- The company's assets are or are likely to be less than its obligations.[22]
- The company is or is likely to be unable to meet its obligations, other than those subject to a bona fide dispute, in the normal course of business.[23]

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[18] Grounds for an FDIC appointment as conservator or receiver are: insufficient assets to meet obligations; dissipation of assets or earnings due to violation of statute or regulation; unsafe or unsound condition to transact business; willful violation of a cease-and-desist order which has become final; concealment of the institution's books or refusal to submit to an inspection or examination; inability to meet obligations; incurring of losses or likelihood of incurring losses that will deplete capital with no reasonable likelihood of becoming adequately capitalized without federal assistance; violation of law or regulation or an unsafe or unsound practice or condition likely to cause insolvency or weaken the institution's condition or seriously prejudice the interests of depositors or the deposit insurance fund; consent—through a board of directors or shareholder resolution; termination of deposit insurance coverage; undercapitalization with no reasonable prospect of becoming adequately capitalized; failing to submit an adequate recapitalization plan or materially failing to implement an accepted capital restoration plan; critical undercapitalization; and conviction of a money laundering offense. CRS Report RL34657, *Financial Institution Insolvency: Federal Authority over Fannie Mae, Freddie Mac, and Depository Institutions*, by David H. Carpenter and M. Maureen Murphy, at 7.

[19] Treasury's March 25, 2009, proposal, § 2(b)(4)(A).

[20] Id., § 2(b)(4)(b). The language of the proposal reads: "[t]he financial company is critically undercapitalized, as such term has been or may be defined by the company's Appropriate Federal Regulatory Agency." Under this proposal, FDIC is the "Appropriate Federal Regulatory Agency" for companies with banks or thrifts in the corporate organization and for holding companies of insurance companies. This raises the question of whether FDIC is to have a greater role in promulgating capital standards for these companies. Currently, there is no federal oversight of insurance companies. Capitalization levels are monitored for bank and financial holding companies and savings and loan holding companies by their primary federal regulator. FRB sets capital standards for bank and financial holding companies. 12 C.F.R. § 225.2(r). OTS " reviews the financial resources of a savings and loan holding company, including capital adequacy, in the examination and supervisory processes. OTS also reviews the financial resources of prospective holding companies in evaluating holding company and other applications, and has the authority to require additional capital on a case-by case basis." 65 Fed. Reg. 64392, 64395 (Oct. 27, 2000).

For a description of bank capital requirements as well as the capital requirements imposed by the SEC and CFTC, see CRS Report R40249, *Who Regulates Whom? An Overview of U.S. Financial Supervision*, by Mark Jickling and Edward V. Murphy, at 7-10

[21] *Id.*, § 2(b)(4)(C).

[22] *Id.*, § 2(b)(4)(D).

[23] *Id.*, § 2(b)(4)(E).

When Is the Systemic Risk Determination Made?

Since the proposal requires that the Systemic Risk Determination include a finding that the financial company is "in default or in danger of default;" it would appear that the proposal does not provide a means of identifying a company or a large group of companies as systemically significant until there are factual circumstances indicating the threat of default.

Who Makes the Systemic Risk Determination?

The proposal requires that the Secretary of the Treasury (the Secretary) make the determination but only after consultation with the President and upon the written recommendation of the Fed and one other federal regulator. The other recommendation must come from the FDIC if the company has an affiliate or subsidiary insured depository institution or insurance company. If there is no insured depository institution or insurance company within the company's corporate organization, there must be a written recommendation from the federal regulator of the company's or affiliate having the largest assets as of the end of the previous calendar year for which unaudited financial statements are available—either the Securities and Exchange Commission (SEC), if the affiliate or subsidiary is a broker or dealer; or the Commodities Futures Trading Commission (CFTC), if the company is an futures commission merchant or a commodity pool operator.[24]

Who Recommends a Systemic Risk Determination?

To initiate the Secretary's Systemic Risk Determination, the Secretary, the Chairman of the Board of Governors of the Federal Reserve System (FRS Board Chairman), or the appropriate federal regulatory agency[25] must request the Board of Governors of the Federal Reserve System (FRS Board), which consists of seven members, all subject to presidential appointment with the advice and consent of the Senate,[26] to make a written recommendation to the Secretary to make a Systemic Risk Determination. For the written recommendation to go forward, it must have the votes of 2/3s of the FRS Board then serving; 2/3s of the FDIC's Board or of the SEC or CFTC [27] as appropriate.

[24] *Id.*, §§ 2(b)(1)((A) and (b), and 1(a)(2).

[25] Under the proposal, the appropriate federal regulatory agency is the FDIC for any company which has as a subsidiary or an affiliate an insured depository institution or an insurance company. If there is no insured depository institution or insurance company within the company's corporate organization, the appropriate federal regulatory agency is the federal regulator of the company's affiliate having the largest assets as of the end of the previous calendar year for which unaudited financial statements are available. That would be the Securities and Exchange Commission (SEC), if the affiliate or subsidiary is a broker or dealer; the Commodities Futures Trading Commission (CFTC), if the company is an futures commission merchant or a commodity pool operator.

[26] 12 U.S.C. § 241. From these members, the President, with the advice and consent of the Senate, appoints a "chairman of the Board" and a "vice-chairman." 12 U.S.C. § 244

[27] The SEC and the CFTC are five-member commissions, each member presidentially appointed with the advice and consent of the Senate, and a chairman, designated from these members by the President with the advice and consent of the Senate. 15 U.S.C. § 78d and 7 U.S.C. § 2(a)(2). The FDIC Board consists of five members—the Comptroller of the Currency, the Director of the Office of Thrift Supervision, and three presidential appointees with the advice and consent of the Senate, one of whom is to be designated by the President with the advice and consent of the Senate, as Chairperson. 12 U.S.C. §§ 1812(a) and (b).

What Must Be Included in the Recommendation for a Systematic Risk Determination?

The recommendation from the FRS Board and the FDIC or SEC or CFTC that the Secretary make a Systemic Risk Determination must include: (1) "a description of the effect that the default of the financial company would have on the economic conditions or financial stability in the United States" and (2) the nature and extent of assistance or actions to be taken or provided by the FDIC regarding the company.[28]

The House Financial Services Committee and the Senate Committee on Banking, Housing, and Urban Affairs must be notified of the determination and its basis. The determination must be documented and retained for review by the Government Accountability Office (GAO), which is to report to Congress within 30 days of the determination. The GAO report is to cover the basis for the determination; the purpose of any action taken; and the "likely effect of the determination and such action on the incentives and conduct of financial companies and their creditors."[29]

What Is the Effect of a Systemic Risk Determination?

Once the Secretary, in consultation with the President, has made the Systemic Risk Determination with respect to a company, the FDIC may take action or actions delegated to the FDIC under this proposal provided the Secretary approves the FDIC's course of action.[30]

What Considerations Must the FDIC Weigh in Determining a Course of Action Once a Systemic Risk Determination Has Been Made?

The two factors which are specified for the FDIC's consideration prior to embarking on a course of resolving the company involve financing and secondary effect. The FDIC must consider: (1) "the cost to the general fund of the Treasury" and (2) "the potential to increase moral hazard on the part of creditors and shareholders in such financial companies."[31]

What Actions May the FDIC Take?

Once a Systemic Risk Determination has been made with respect to a company, the proposal provides the FDIC with authority to take any or all or any combination of specified actions "with the approval of the Secretary" and "under such terms and conditions that the ... [FDIC] deems appropriate." The actions specified are:

- Lending or purchasing the debt obligations of the company or any of its subsidiaries.

[28] Treasury's March 25, 2009, proposal, § 1(b)(2).

[29] *Id.*, § 2(b)(3).

[30] *Id.*, § 2(b)(2).

[31] *Id.*, § 2(b)(2).

- Purchasing the assets of the company or any of its subsidiaries.
- Acquiring an equity interest or security of the company or any of its subsidiaries.
- Taking a lien on assets of the company or any of its subsidiaries, "including a first priority lien on all unencumbered assets of the company or any subsidiary."
- Selling or transferring any acquired assets, liabilities, obligations, equity interests, or securities of the company or any of its subsidiaries upon terms that the FDIC deems appropriate.
- Appointing itself as conservator or receiver for the company. [32]

Language of the proposal declares that any company which is placed into conservatorship or receivership or receives assistance under the resolution authority of this proposal "is not an agency, establishment, or instrumentality of the United States for purposes of statutes that confer powers on or impose obligations on government entities." It further states that the employees of such companies are not, as such, officers or employees of the United States, but that FDIC employees and other federal employees who serve as its employees or officers shall not lose their status as officers or employees of the United States or receive any additional salary with respect to their service as employees of such a company [33]

What Rulemaking Authority is Provided Under this Proposal?

Rulemaking authority is to be exercised jointly by the FDIC and the Secretary. It extends to promulgating "such rules or regulations as they consider necessary or appropriate to implement the provisions of this section," i.e., the resolution authority provisions.[34]

What Are Some of the Effects of FDIC's Appointment as Receiver or Conservator?

Judicial Review and Effect on Other Litigation

This proposal provides limited judicial review. FDIC's appointing itself as conservator or receiver for a company after a Systemic Risk Determination may be challenged, but the action to remove the conservator or receiver must be filed in the federal district court of the "home office"[35] of the

[32] *Id.*, § 2(c). FDIC's conservatorship or receivership authority for depository institutions are set forth briefly in CRS Report RL34657, *Financial Institution Insolvency: Federal Authority over Fannie Mae, Freddie Mac, and Depository Institutions*, by David H. Carpenter and M. Maureen Murphy, at 8-11.

[33] *Id.*, § 2(w).

[34] This seems to include authority to promulgate rules regarding both the operation of receiverships and conservatorships or assistance packages and the process of making Systemic Risk Determinations. It may also include authority to establish capital requirements for companies not currently under such requirements or to establish triggering mechanisms for monitoring financial companies in terms of systemic risk—narrowing the number of institutions in terms of size, influence, etc., on which the focus will fall. It is possible that not all companies classified as financial holding companies need to be scrutinized for systemic risk. FRB's list of financial holding companies lists 810 companies as of March 27, 2009. http://www.federalreserve.gov/generalinfo/fhc/.

[35] Although "home office" is a concept used with respect to depository institutions, "place of incorporation" or "principal place of business" is generally used for other types of corporations. See, e.g., 28 U.S.C. § 1332(c)(1), the federal diversity-of-citizenship statute, which proclaims, in pertinent part, that "a corporation shall be deemed to be a (continued...)

company within 30 days of the appointment. [36] It also insulates directors of the company from liability to the company's shareholders or creditors for acquiescing to the conservatorship or receivership or to the FDIC's "acquisition, combination, or transfer of assets or liabilities."

An FDIC conservatorship or receivership terminates and precludes the initiation of any bankruptcy case or state insolvency proceeding with respect to the company.[37]

General Resolution Powers

As conservator or receiver, the FDIC becomes the successor to the company and succeeds to its rights and those of its stockholders, officers, and directors, and to any assets of a previous receiver or other legal custodian of the company.[38] It is endowed with "all the powers of the members or shareholders, the directors, and the officers" of the company. It "may conduct all the business" of the company; and, with the approval of the Secretary, make loans to, purchase the assets of, assume or guarantee the obligations; or acquire an equity interest in or a security of the company or any of its subsidiaries. It may collect all the obligations due to the company, perform its functions; and preserve and conserve its assets; and contract for assistance.[39]

As conservator, the FDIC may "subject to all legally enforceable and perfected security interests" in the company's assets, take any action necessary to make the company sound and solvent and appropriate to carry on its business and preserve and conserve its assets and property.[40]

As receiver, the FDIC may place the company in liquidation and realize upon its assets, as the FDIC deems appropriate. This includes selling assets; transferring assets to a bridge financial company; or exercising any of the specific powers granted to the receiver under this proposal.[41] It may also organize a bridge financial company.[42]

There are also accounting and recordkeeping requirements, including a publicly available annual accounting and a full accounting of each receivership or conservatorship.[43]

A provision requires the appropriate federal regulatory agency[44] to make available all supervisory records which the receiver may use in any manner.[45]

(...continued)

citizen of any state by which it has been incorporated and of the State where it has its principal place of business."

[36] Treasury's March 25, 2009, proposal, § 1(d).

[37] *Id.*, §§ 2(f) and (g).

[38] *Id.*, § 2(h)(1)(A).

[39] *Id.*, § 2(h)(1)(B).

[40] *Id.*, § 2(h)(1)(D).

[41] *Id.* § 2(h)(1)(E).

[42] *Id.* § 2(h)(1)(F). Bridge financial company authority is describe *infra*, text surrounding n.111-117.

[43] *Id.*, § 2(h)(16).

[44] Under the proposal, the appropriate federal regulatory agency is the FDIC for any company which has as a subsidiary or an affiliate an insured depository institution or an insurance company. If there is no insured depository institution or insurance company within the company's corporate organization, the appropriate federal regulatory agency is the federal regulator of the company's affiliate having the largest assets as of the end of the previous calendar year for which unaudited financial statements are available. That would be the Securities and Exchange Commission (SEC), if the affiliate or subsidiary is a broker or dealer; the Commodities Futures Trading Commission (CFTC), if the company (continued...)

Merger Authority and Asset-Transfer Authority of Conservator or Receiver

The FDIC may merge the company with another company or transfer any of its assets or liabilities, including those associated with a trust or custody business. If a merger requires approval by another federal agency, the transaction may not be consummated until the fifth day after that agency's approval. If a report on competitive factors is required, the Attorney General must be notified promptly and provide the report within ten days of the request. If a filing under the Hart-Scott-Rodino Antitrust Improvements Act of 1976[46] is required, the waiting period must expire no later than 30 days after the filing. In the event of a finding by the Secretary, in consultation with the Chairman of the FRS Board, that the transaction must occur immediately "to prevent the probable failure of one or more of the financial companies for which there has been a Systemic Risk Determination, the FDIC may consummate the transaction.[47]

Miscellaneous Powers; Incidental Powers; and Termination of Shareholders' Rights

The proposal provides the FDIC as receiver or conservator with authority to pay the obligations of the company "due and payable" at the time the FDIC is appointed, provided the "prescriptions and limitations" set forth are observed. It authorizes the FDIC to issue subpoenas and provides it with authority to compel testimony and the attendance of witnesses, and subjects violations to potential criminal penalties.[48] It provides the FDIC with authority to employ the private sector in managing and disposing of the assets of the company—provided that the services are available in the private sector and the FDIC determines that to use them would be "practicable, efficient, and cost effective."[49] In addition to the explicit powers granted to the FDIC as conservator or receiver, the proposal contains a provision delegating to the Corporation as receiver or conservator "such incidental powers as shall be necessary to carry out such powers."[50] There is also a provision stating that the FDIC is to terminate all rights and claims of stockholders and creditors of the company except to their right to any satisfaction as specified in the proposal.[51]

Judicial Proceedings

A specific provision in the proposal limits the ability of courts to restrain the conservator or receiver to the specifics of this proposal.[52]

(...continued)

is a futures commission merchant or a commodity pool operator.

45 *Id.*, § 2(p).

46 This law provides for premerger notification. 15 U.S.C. § 18a.

47 *Id.*, § 2(h)(1)(G).

48 *Id.*, § 2(h)(1)(I), incorporating by reference 12 U.S.C. § 1818(n).

49 *Id.*, § 2(h)(1)(K).

50 *Id.*, § 2(h)(1)(J).

51 *Id.*, § 2(h) (1)(L).

52 *Id.*, § 2(l). It states: "[e]xcept as provided in this section or at the request of the conservator or receiver appointed for a covered financial company under this section, no court may take any action to restrain or affect the exercise of powers or functions of the conservator or receiver hereunder."

FDIC Rights and Remedies

The proposal specifies that the FDIC must abide by a final judgment rendered before its appointment as conservator or receiver. It provides the FDIC with various rights and remedies with respect to other litigation. The FDIC succeeds to all rights and remedies of the company and to any that it enjoys in its own capacity, including the right to remove a case to federal court. In addition, the FDIC may not be required to post bond; its assets may not be attached; and judicial review is limited to that specified in this proposal with respect to:

> (i) any claim or action for payment from, or any action seeking a determination of rights with respect to, the assets of any covered financial company for which the Corporation has been appointed receiver, including any assets which the Corporation may acquire from itself as such receiver; or
>
> (ii) any claim relating to any act or omission of such covered financial company or the Corporation as receiver.[53]

There are also provisions permitting the FDIC to obtain (in federal court, and under certain circumstances, in state court) injunctive relief under Rule 65 of the Federal Rules of Civil Procedure without having to show irreparable harm. This could include attaching the assets of any person and placing them under the control of a court-appointed trustee.[54]

Priority over other claims is specified for court-ordered money damages imposed upon the FDIC by a final judgment for breach of an agreement by the company and approved by the FDIC. Such damages are to be paid as an administrative expense of the receivership or conservatorship.

When Must Actions Against FDIC As Conservator or Receiver Be Filed?

The statute of limitation for tort claims is three years from when the claim accrues; six years for contract claims. In either case, the period specified in the applicable state statute may be used, if it provides a longer time. This period begins to run on whichever date is later: when the FDIC was appointed receiver or conservator or the date on which the cause of action accrues. the FDIC may bring a tort claim based on intentional misconduct resulting in unjust enrichment or substantial loss to the covered company, despite expiration of the claim under the applicable state statute, provided that it has expired not more than five years before the appointment of FDIC.[55]

Fraudulent Transfers

The fraudulent transfer provision applies to transfers by institution-affiliated parties[56] or debtors of the company made within five years of the FDIC's appointment as conservator or receiver

[53] *Id.*, § 2(h)(10)(D).

[54] *Id.*, §§ 2(h)(13 and 14).

[55] *Id.*, § 2(h)((11).

[56] A definition is provided for "institution-affiliated party" that tracks the language of 18 U.S.C. § 1813(u), which defines "institution-affiliated party" for purposes of the FDI Act. One difference is that, although this provision extends to independent contractors of the company who knowingly or recklessly participate in a violation of "any unsafe or unsound practice," there appears to be no definition of "unsafe or unsound practice" for companies which are not banks or thrifts or their holding companies.

provided there was intent to hinder, delay, or defraud the company. It permits the FDIC to recover fraudulent transfers from the initial transferee or any immediate or mediate transferee of that tranferee except for any transfer from the initial transferee or another transferee made for value and in good faith.[57]

Expedited Procedures for Appeals in Cases Against Directors, Etc.

The proposal specifies that any appeal of an order in a case brought by the FDIC against "a director, officer, employee, agent, attorney, accountant, or appraiser or any other person employed by or providing services" to a company for which a Systemic Risk Determination has been made must be filed within 30 days of the date of the entry of the order and the appeal hearing held within 120 days thereafter. This schedule is subject to modification by a federal court in a particular case upon a finding that "the ends of justice that would be served by making such a modification would outweigh the best interest of the public in having the case resolved expeditiously."[58]

There is also a provision permitting the FDIC to request assistance of any foreign financial authority and to maintain an office to coordinate foreign investigations.[59]

There is also a provision precluding the FDIC from entering into an agreement or protective order preventing the disclosure of the terms of a settlement for money damages or restitution in an action brought in its capacity as a conservator or receiver for a company for which a Systemic Risk Determination has been made.[60]

What Standards Are Imposed Upon FDIC As Conservator or Receiver Under This Proposal?

The proposal imposes some general obligations upon the FDIC as conservator or receiver. It must conduct its operations to maximize the return from sale or disposition of assets; minimize the amount of loss in resolving cases; minimize the cost to the Treasury; mitigate the "potential for serious adverse effects to the financial system and the U.S. economy"; ensure "timely and adequate competition and fair and consistent treatment of offerers"; and prohibit discrimination on the basis of race, sex, or ethnic groups in the solicitation and consideration of offers.[61]

How Are Claims Determined?

Overview

The proposal provides the FDIC, within any limits specified elsewhere in the proposal, with a general set of claim priorities, procedures, and powers to administer a receivership of a company

[57] *Id.*, § 2(h)(12).

[58] *Id.*, § 2(q).

[59] *Id.*, § 2(r). This incorporates by reference the authority of the FDIC to seek foreign supervisory cooperation with respect to FDIC supervision of banks. 12 U.S.C. § 1818(v).

[60] *Id.*, § 2(t).

[61] *Id.*, § 2(h)(1)(E).

after a systemic risk determination.[62] It authorizes the FDIC to use its current conservatorship/receivership regulations[63] as if the company were an insured depository institution in receivership.[64]

As receiver, the FDIC is responsible for settling claims against the institution. The funds for settling creditors' claims are the proceeds from the sale and liquidation of the company's assets. Creditors are notified that they must present their claims within a certain time frame, which may not be less than 90 days from the date of the notice. Within 180 days[65] of receiving a claim, the FDIC must notify the claimant of whether or not it will allow the claim.[66] The FDIC has authority to disallow claims "not proved to the satisfaction of the receiver."[67] Claims not filed within the 90-day period are to be disallowed, subject to an exception for claimants who did not receive notice in time, provided payment is possible.[68] When a claim has been disallowed, the claimant has 60 days to seek administrative or judicial review or the claim is deemed disallowed.[69] FDIC is required to establish an expedited procedure to handle claims by claimants alleging enforceable or perfected security interests in assets and irreparable injury should their claims be handled by the routine process.[70] A special rule applies regarding payments to less than fully secured creditors—any portion of the claim not satisfied by the fair market value of the secured asset is to be treated as an unsecured claim and not paid except in connection with the disposition of all claims by unsecured creditors.[71] No judicial review is permitted of a determination to disallow a portion of a claim or to treat anything above the fair market value of the asset securing a claim as an unsecured claim.[72] Filing a claim is deemed to be commencement of an action for purposes of tolling any statute of limitations.[73]

Under this proposal, the FDIC, as receiver, has the power to defeat claims against its interests in assets it has acquired in a receivership or conservatorship. To prevail on a claim that tends to defeat or diminish the FDIC's interest in such an asset, the claimant must show that there was a written agreement, executed by an authorized officer or representative of the company, which is in receivership.[74]

[62] *Id.*, § 2(h)(2).

[63] 12 C.F.R., Part 360 (issued under the authority of the FDI Act, 12 U.S.C. §§ 1811-1835a).

[64] Treasury's March 25, 2009 proposal § 2(h)(3).

[65] There is a provision permitting an extension of the time for determining whether to allow a claim; it requires a written agreement with the FDIC. *Id.*, § 2(h)(4)(A).

[66] *Id.*, § 2(h)(4)(A).

[67] *Id.*, § 2(h)(4)(b)(B).

[68] *Id.*, § 2(h)((4)(C).

[69] *Id.*, § 2(h)(5).

[70] *Id.*, § 2(h)(6). Under this procedure, the FDIC must make a determination within 90 days of the filing of the claim as to whether to allow or disallow the claim or submit it to the routine procedures. The claimant has a right to file a judicial action upon denial of the claim or when 90 days have elapsed from the filing of the claim for expedited review. *Id.*, §§ 2(h)(6)(B) and (C).

[71] *Id.*, § 2(h)(4)(F)(i). Claims by a Federal Reserve bank or by the Secretary of the Treasury are not subject to the FDIC's authority to disallow any portion of claim or to treat any excess over the fair market value of the secured property as an unsecured claim. *Id.*, § 2(h)(4)(D)(iii).

[72] *Id.*, § 2(h)(4)(E).

[73] *Id.*, § 2(h)(4)(F)(i).

[74] *Id.*,§ 2(h)(7). This is based on one of the powers given to FDIC both as a conservator or receiver of a failed depository institution and in its corporate capacity under 12 U.S.C. § 1823(e). Under that provision, the claimant must (continued...)

The proposal grants the FDIC discretion to pay dividends on proven claims without liability to any claimant whose claim is not proved at the time of the payment; it also provides the FDIC with authority to issue rules "to establish a single uniform interest rate for, or to make payments of post insolvency interest to creditors holding proven claims ... following satisfaction by the receiver of the principal amount of all creditor claims."[75]

What is the Maximum Liability to a Claimant?

The proposal sets FDIC's maximum liability as a receiver "or in any other capacity" at the amount a claimant would have received if there had not been a Systemic Risk Determination and the company had been liquidated in bankruptcy court or under state insolvency law. It does, however, permit the FDIC, with the approval of the Secretary of the Treasury, to make additional payments if it determines that doing so will minimize losses to the receivership or "prevent or mitigate serious adverse effects to financial stability or the U.S. economy." [76]

Priority of Claimants

To the extent that funds are available, the FDIC as receiver is to pay all claims of the same class on a pro rata basis. In a receivership, secured claims take precedence over any unsecured claims and are to be paid to the extent of the security. Any liability beyond what is secured is handled as an unsecured claim. The proposal specifies the order in which unsecured claims are to be discharged, i.e., paid, from the receipts of the liquidation. It specifies the following priority for payment of unsecured claims that are proven to the satisfaction of the receiver:

- Administrative expenses of the receiver.[77]
- Any amounts owed to the United States.
- Any other general or senior liability.
- Any obligation subordinated to depositors or general creditors which is not an obligation owed to shareholders as shareholders.
- Obligations owed to shareholders arising as a result of their status as shareholders.[78]

Although the general rule requires similar treatment of creditors similarly situated, there are exceptions, provided that all similarly situated claimants receive no less than they would have received had the company been liquidated either in bankruptcy court or in state court, without the

(...continued)

show that there was a written agreement, executed contemporaneously with the institution's acquisition of the assets, approved by the institution's board of directors or its loan committee, and continuously reflected on the institution's books.

[75] *Id.*, §§ 2(h)(8)(B) and (C).

[76] *Id.*, § 2(k).

[77] A definition is provided for "administrative expenses of the receiver" which includes "any obligations that the receiver determines are necessary and appropriate to facilitate the smooth and orderly liquidation or other resolution of the covered financial company." *Id.*, § 2(i)(3(B).

[78] *Id.*, § 2(i)(1).

Systemic Risk Determination.[79] The FDIC is permitted to depart from the requirement to treat all similarly situated claimants alike if it makes a determination with respect to the need to do so for certain reasons. These include: maximizing return on assets and containing potential adverse effects upon the U.S economy.[80]

Contracts Entered Into Before Appointment of Conservator or Receiver

The proposal authorizes FDIC, as conservator or receiver, to repudiate any contract or lease to which the company is a party, which the FDIC, in its discretion, determines to be burdensome and that repudiating it will promote the orderly administration of the company's affairs. Repudiation must be within a reasonable time following the FDIC's appointment. Liability for repudiation is limited to "actual direct compensatory damages" as of the date of the conservatorship or receivership, and with respect to certain "qualified financial contracts,"[81] the date of the repudiation. There can be no punitive or exemplary damages or damages for lost profits, lost opportunity, or for pain and suffering.[82] For "qualified financial contracts," compensatory damages are "to include normal and reasonable costs of cover or other reasonable measures of damages utilized in the industries for such contract and agreement claims."[83]

Leases or Contracts for the Sale of Real Property and Service Contracts

If the FDIC, as conservator or receiver, repudiates a lease of which the company was a lessee, unless the lessor is in breach of the terms of the lease, damages shall be limited to the contractual rent accruing before the later of (1) the date the notice of repudiation is mailed or (2) the date the repudiation becomes effective. There may be no claim for damages under any penalty provision or acceleration clause and offsets are allowable.[84]

If the company is the lessor and the FDIC repudiates a lease of real property, provided the lessee is not in default, the lessee may treat the lease as terminated by the repudiation or remain in possession for the balance of the lease and continue to pay the contractual rent and offset any damages accruing after the date of repudiation against any rent payment. No damages arising after the date of the repudiation will be allowable other than offsets for damages occurring after

[79] *Id.*, § 2(i)(2), incorporating by reference § 2(k)(2).

[80] *Id.*§ 2(i)(2). The provision requires that the FDIC determine that such action is necessary for purposes of maximizing the return on the company' assets. To depart from this standard, the FDIC must determine that making payments that do not meet this requirement "is necessary to maximize the value of the assets of the covered financial company, to maximize the present value return from the sale or other disposition of the assets of the covered financial company, to minimize the amount of any loss realized upon the sale or other disposition of the asserts of the covered financial company, or to contain or address serious adverse effects on the financial stability or the U.S. economy."

[81] A "qualified financial contract," is defined, for these purposes, to mean "any securities contract, commodity contract, forward contract, repurchase agreement, swap agreement and any similar agreement that ... [the FDIC] determines by regulation, resolution, or order to be a qualified financial contract.... " *Id.*, § 2(i)(8)(D)(i).

[82] *Id.*, § 2(j)(3)(b).

[83] *Id.*, § 2(j)(3)(C). The proposal sets some standards for payment of a "qualified financial contract."

[84] *Id.*, § 2(i)(4).

the date of repudiation due to the nonperformance of an obligation of the company under the lease after that date.[85]

If the FDIC, as conservator or receiver, repudiates a contract for the sale of real property, that is in writing and executed by an authorized officer or representative of the company, if the purchaser is in possession and not in default, the purchaser may treat the contract as terminated or remain in possession. Purchasers choosing to remain in possession are entitled to having the FDIC deliver title to them; they must continue to make all payments due under the contract and may offset against such payments any damages accruing after the date of repudiation that are due to the nonperformance of any obligation of the company. No damages arising after the date of the repudiation will be allowable other than offsets for damages occurring after the date of repudiation due to the nonperformance of an obligation of the company under the contract after that date. Despite the existence of the contract, the FDIC is authorized to sell or assign the contract.[86]

Service contracts involving services performed for the company before the appointment of the FDIC as receiver or conservator are deemed to have arisen on the date of the FDIC's appointment and are to be paid in accordance with the conservatorship and receivership rules. For services performed after the appointment of the FDIC, if the FDIC does not exercise the right of repudiation, the counterparty shall be paid according to the terms of the contract as an administrative expense of the conservatorship or receivership. The FDIC may subsequently repudiate the contract.[87]

How Are "Qualified Financial Contracts" Treated?

Under the proposal, "qualified financial contracts" are treated similarly to the way they are treated in the case of an FDIC bank conservatorship or receivership. The FDIC has no authority to stay or prevent (beyond 5 p.m., eastern time, of the day following the appointment of the receiver)[88] the exercise by a party to a "qualified financial contract" of any rights under any credit enhancement or offset or netting agreement arising upon the appointment of the FDIC as a receiver.[89] If FDIC is appointed as conservator, counterparties to "qualified financial contracts" may not exercise rights to "terminate, liquidate, or net" such contracts "solely by reason of or incidental to the appointment of ... a conservator."[90] A "qualified financial contract" is defined as "any securities contract, commodity contract, forward contract, repurchase agreement, swap agreement, and any similar agreement that the ... [FDIC] determines by regulation, resolution, or order to be a qualified financial contract."[91] This term covers "derivative master agreements," which "contain close-out provisions which, when triggered, allow the solvent counterparty to immediately terminate the contract (and all transactions under the master agreement), net the values, and pay the net amount due or file a claim if the net amount is owed."[92] Definitions are

[85] *Id.*, § 2(j)(5).

[86] *Id.*, § 2(j)(6).

[87] *Id.*, § 2(j)(7).

[88] *Id.*, § 2(j)(10)(B)(i). Compare 12 U.S.C. § 1821(e)(10)(B)(i).

[89] *Id.*, § 2(j)(8)(A). Compare 12 U.S.C. § 1821(e)(8)(A).

[90] *Id.*, § 2(j)(10)((B)(ii). Compare 12 U.S.C. § 1821(e)(10)(B)(ii).,

[91] *Id.*, § 2(j)(8)D)(i).

[92] Robert R. Bliss and George G. Kaufman, "U.S. Corporate and Bank Insolvency Regimes: A Comparison and Evaluation," 2 *Va. L. & Bus. Rev.* 144, 158. (2007).

supplied for "securities contract," "commodity contract," "forward contract," "repurchase agreement," and "swap agreement," which are virtually[93] identical to those provided in the FDI Act.[94]

There are also definitions of "default" and "in danger of default"[95] for purposes of the provisions permitting parties to enforce "qualified financial contracts." These definitions also apply to the provisions requiring the FDIC as conservator or receiver to supply notice when transferring any "qualified financial contracts" of a company for which a Systemic Risk Determination has been made. The definitions closely parallel those found in the FDI Act.[96]

Master agreements are treated similarly to their treatment under the FDI Act. A master agreement with any supplements is to be treated as one "qualified financial contract" minus any provision not, in itself, a "qualified financial contract."[97]

As in the FDI Act, a separate provision provides clarification that the FDIC retains the power to transfer and to repudiate qualified financial contracts within the limits established.[98] There are also parallel provisions specifying that walkaway clauses are not enforceable against a company for which a Systemic Risk Determination has been made that is in default and authorizing the FDIC to prescribe recordkeeping rules with respect to qualified financial contracts.[99] Other provisions govern transfer of qualified financial contracts and notification of those transfers.[100] One provision requires the FDIC to repudiate all or none of the "qualified financial contracts" between the company for which a Systemic Risk Determination has been made and any person or any affiliate of that person.[101]

There is a provision preventing the FDIC from avoiding legally enforceable or perfected security interests except where taken in contemplation of the company's insolvency or with intent to hinder, delay or defraud the company or the creditors of the company.[102]

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[93] There is one variation. In the definition of "repurchase agreements," the proposal confines its applicability with respect to repurchase agreements of qualified foreign government securities to any "security that is a direct obligation of, or that is fully guaranteed by, the central government of the Organization for Economic cooperation and Development as determined by regulation or order adopted by the Federal Reserve Board." Treasury's March 25, 2009, proposal, § 2(j)(8)(D)(v)(I). The provision in the FDI Act refers to "the appropriate Federal banking authority," rather than to the Federal Reserve Board alone. 12 U.S.C. § 1821(e)(9)(v).

[94] 12 U.S.C. § 1821(e).

[95] Treasury's March 25, 2009, proposal, § 2(j)(8)(D)(vii).

[96] 12 U.S.C. § 1813(x). Aside from the differences relating to the deposit insurance fund, one difference is that the proposal's definition of "in danger of default" requires a determination by the FDIC or the "appropriate State authority" that the company is not likely to pay its obligations in the normal course of business or that it will be able to do so without federal assistance. The FDI Act refers to the "appropriate federal banking agency" or the FDIC.

[97] Treasury's March 25, 2009, proposal, §2(j)(8)(D)(viii). Compare 12 U.S.C. § 1821(e)(8)(vii).

[98] *Id.*§ 2(j)(8)F). The clarification reads: "No provision of law shall be construed as limiting the right or power of the ... [FDIC], or authorizing any court or agency to limit or delay, in any manner, the right or power of the .. [FDIC] to transfer any qualified financial contract in accordance with paragraphs 9 and 10 [transferring qualified financial contracts and notification of transfer] or to repudiate any such contract in accordance with subsection (j)(1) [allowing repudiation of burdensome contracts the repudiation of which the conservator or receiver determines to be burdensome].

[99] *Id.*, §§ 2(j)(8)(G) and (H).

[100] *Id.*, §§ 2(j)(9) and (10). Compare 12 U.S.C. §§ 1821(e)(9) and (10).

[101] *Id.*, § 2(j)(11). Compare 12 U.S.C. § 1821(e)(11).

[102] *Id.*, § 2(j)(12). Compare 12 U.S.C. § 1821(e)(12).

Authority to Enforce Contracts

Specific authority, similar to that in the FDI Act, is provided to the FDIC to "enforce any contract, other than a director's or officer's liability insurance contract or a financial institution bond"[103] entered into by the company for which a Systemic Risk Determination has been made notwithstanding a contractual clause providing for termination, default, acceleration, or exercise of rights upon, or solely by reason of insolvency or the appointment of or the exercise of rights or powers by a conservator or receiver.[104]

For 45 days after the appointment of a conservator or 90 days after the appointment of a receiver, counterparties may not, without the consent of the FDIC, assert rights to terminate, accelerate, or declare a default on a contract without the consent of the FDIC as conservator or receiver.

Exceptions apply to certain "qualified financial contracts," netting arrangements,[105] and director or officer liability insurance contracts or financial institution bonds.[106]

There is also an exception for Federal Reserve bank credit or security interests securing such extensions of credit.[107]

Liability of Directors and Officers

The proposal, in language similar to that in the FDI Act,[108] provides for personal liability in money damages for directors or officers of a company for which there has been a Systemic Risk Determination in a civil action by the FDIC as conservator or receiver based on gross negligence or intentional tortious conduct as defined under applicable state law.[109] This applies to any suit brought by the FDIC, or on behalf of the FDIC, either as conservator or receiver or as the assignee of a company for which the FDIC has provided assistance under the provisions of this proposal.[110]

A separate section specifies that damages in actions against a "director, officer, employee, agent, attorney, accountant, or appraiser, or any other party employed by or providing services to" a company for which a Systemic Risk Determination has been made are to include principal losses resulting from "improvident or otherwise improper use or investment of ... assets" and interest.[111]

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[103] These may be enforced under other applicable law.

[104] *Id.*¸ § 2(j)(12). Compare 12 U.S.C. § 1821(e)(13).

[105] Netting arrangements covered under 12 U.S.C. §§ 4401-4407 are excepted from this rule.

[106] Treasury's March 25, 2009, proposal, § 2(j)(13).

[107] *Id.*, § 2(j)(14).

[108] 12 U.S.C. § 1821(l). In *Atherton v. FDIC*, 519 U.S. 213 (1997), the U.S. Supreme Court held that the gross negligence standard of care in this statute is a floor and that states are free to enact statutes holding directors and officers liable on a showing of negligence. The Court noted the existence of the savings clause as preserving state laws to which the FDIC may turn, which also appears in Treasury's March 25, 2009, proposal, at § 2(m)(3). It reads: "Nothing in this paragraph shall impair or affect any right of the ... [FDIC] under any other applicable law."

[109] Treasury's March 25, 2009, proposal, § 2(m).

[110] Treasury's March 25, 2009, proposal, § 2(m).

[111] *Id.*, § 2(n). Compare 12 U.S.C. § 1821(l).

Bridge Financial Companies

Establishment and Duration

The proposal provides that FDIC, as receiver of one or more companies for which a Systemic Risk Determination has been made, or anticipating appointment as receiver of one or more such companies, may organize a bridge financial company (BFC).[112] Such a BFC may assume the liabilities of a company for which there has been a Systemic Risk Determination, purchase its assets, or perform any other function that the FDIC in its discretion may prescribe in accordance with the provision of this proposal. The aggregate amount of liabilities from the company that are transferred to the BFC may not exceed the amount of the company's assets transferred to or purchased by the BFC.[113] The FDIC may issue a BFC charter, the effect of which is to immediately establish such a company, which is to be under the direction of a board of directors appointed by the FDIC, with articles of association and an organization certificate with terms established by the FDIC. FDIC may provide for the BFC to succeed to and assume the rights and powers of the company for which it has been established.[114] The BFC may operate without any capital or surplus. The FDIC is not required to supply the BFC with any capital or to issue stock on its behalf; but it may cause capital stock or other securities of a BFC to be issued and offered for sale. The BFC "shall not assume ... any obligation ... to any shareholder ... [of the company for which it has been established] that arises as a result of the status of that person as a shareholder."[115] There is also a provision authorizing the FDIC to dissolve the BFC at any time as the receiver of the BFC and specifying that "in the exercise of such rights, powers, and privileges the ... FDIC ... shall not be subject to the direction or supervision of any State agency or Federal agency."[116]

BFC's are temporary in nature and may exist no longer than five years. A BFC's charter is limited to two years with possibility of FDIC extending it for three additional one-year periods.[117]

The proposal specifies that a BFC must terminate whenever one of the following events occurs: merger with a non BFC; at the election of the FDIC, the sale of a majority of the BFC's capital stock to a non-BFC; sale of 80 percent or more of the BFC's capital stock to a person other than the FDIC or another BFC; at the election of the FDIC, the assumption of substantially all of the BHC's liabilities or acquisition of substantially all of its assets by a non-BFC; the expiration of the five-year period; or the dissolution of the BFC.[118]

[112] The provisions pertaining to bridge financial companies parallel those in the FDI Act with respect to bridge depository institutions, 12 U.S.C. § 1821(n), with at least one important distinction—bridge depository institutions receive national bank charters from the agency which charters all national banks, the Office of the Comptroller of the Currency, and are subject to the National Bank Act, rather than the corporate law of any state.

[113] Treasury's March 25, 2009, proposal, § 2(o)(5)(F).

[114] *Id.*, §§ 2(o)(1) and (2).

[115] *Id.*, § 2(o)(3)(B).

[116] *Id.*, § 2(o)(14).

[117] *Id.*, §§ 2(o)(11) and (12).

[118] *Id.*, § 2(o)(11) and (12). The proposal includes specifications as the legal effect of each of these termination events. *Id.*, § 2(o)(13).

Stay of Judicial Action

The BFC may request a stay of up to 45 days (or longer, upon consent of the other party) of any judicial action to which it becomes a party by acquiring assets or liabilities of a company for which a Systemic Risk Determination has been made.[119]

A BFC may be treated as a company for which there has been a Systemic Risk Determination for such purposes as the FDIC may determine. FDIC may transfer any assets and liabilities of any such company to a BFC, without any further approval under state or federal law. In transferring assets and liabilities, FDIC is subject to a general rule to treat all similarly situated creditors in a similar manner. There is an exception if FDIC determines that other actions are necessary to maximize the value of the assets or the return from the sale of assets or to minimize the amount of loss or "contain or address serious adverse effects to financial stability or the U.S. economy." In that case, all creditors receive the amount that they would have been entitled to had the company been liquidated under the bankruptcy code or under state insolvency law.[120]

What Corporate Law Applies to a Bridge Financial Company?

The BFC, as permitted by the FDIC and in conformity with the provisions of the proposal, may "elect to follow the corporate governance practices and procedures as are applicable to a corporation incorporated under the general corporation law of the State of Delaware, or the state of incorporation or organization" of the company for which it was established "as such law may be amended from time to time."[121]

Agreements Against the Interest of a Bridge Finance Company

Under this proposal, the BFC may defeat claims against its interests in assets transferred from the company for which there has been a Systemic Risk Determination. To prevail on a claim that tends to defeat or diminish the BFC's interest in such an asset, the claimant must show that there was a written agreement executed by an authorized officer or representative of the company.[122]

Bridge Financial Companies: Not Federal Agencies and Are Tax-Exempt

The provision declares that a BFC has tax exempt-status and "is not an agency, establishment, or instrumentality of the United States," and that its employees are not, as such, officers or employees of the United States, but that FDIC employees and other federal employees who serve as employees or officers of a BFC shall not lose their status as officers or employees of the

[119] *Id.*, § 2(o)(6).

[120] *Id.*, § 2(o)(5).

[121] *Id.*, § 2(o)(2)(F).

[122] *Id.*, § 2(o)(7). Compare *Id.*,§ 2(h)(7). This is based on one of the powers given to FDIC both as a conservator or receiver of a failed depository institution and in its corporate capacity under 12 U.S.C. § 1823(e). Under that provision, the claimant must show that there was a written agreement, executed contemporaneously with the institution's acquisition of the assets, approved by the institution's board of directors or its loan committee, and continuously reflected on the institution's books. A similar provision applies to bridge banks. 12 U.S.C. § 1821(n)(4)(I).

United States or receive any additional salary with respect to their service as employees of a BFC.[123]

If a merger or sale of a BFC requires approval by another federal agency, the transaction may not be consummated until the fifth day after that agency's approval. If a report on competitive factors is required, the Attorney General must be notified promptly and provide the report within ten days of the request. If a filing under the Hart-Scott-Rodino Antitrust Improvements Act of 1976[124] is required, the waiting period must expire no later than 30 days after the filing. In the event of a finding by the Secretary, in consultation with the Chairman of the FRB, that the transaction must occur immediately "to prevent the probable failure" of one or more of the financial companies for which there has been a Systemic Risk Determination, the FDIC may consummate the transaction.[125]

Authority of Bridge Financial Company to Obtain Credit

The proposal authorizes a BFC to obtain unsecured credit and issue unsecured debt and provides the FDIC with authority to authorize a BFC to obtain credit or issue debt. The credit or debt may have priority over all other obligations of the BFC; it may be secured by a lien on the BFC's property not otherwise encumbered; or it may be secured by a junior lien on property subject to a lien. To approve a proposal for a BHC to obtain credit or issue debt secured by an existing lien, the FDIC must find that the BHC is unable to obtain credit otherwise and that there is adequate protection for the interest of the existing lien holder. The FDIC carries the burden of proof on the issue of adequate protection.[126]

Liquidation of Certain Stockbrokers or Commodity Brokers

If a company which is liquidated following a Systemic Risk Determination, is a stockbroker that is not a member of the Securities Investor Protection Agency or a commodity broker, FDIC must apply the provisions of subchapter III of chapter of title 11 in respect to the distribution to any "customer" of "customer name securities" and "customer property" as those terms are defined in 11 U.S.C. § 761.[127]

Funding for FDIC's Resolution Authority

The proposal provides an authorization of appropriation of "such sums as are necessary, without fiscal year limitation," but "subject to apportionment under 31 U.S.C. § 1517, and to the restrictions that generally apply to the use of appropriated funds in title 31, United States Code, and other laws." Any FDIC receipts in carrying out this resolution authority, except for receipts when in its capacity as conservator or receiver of a company, are to be deposited in the Treasury's general fund.[128]

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[123] *Id*, §§ 2(o)(8) and (9).

[124] This law provides for premerger notification. 15 U.S.C. § 18a.

[125] *Id.*, § 2(o)(10).

[126] *Id.*, § 2(o)(15).

[127] *Id.*, § 2(t).

[128] *Id.*, § 2(u). To resolve bank and thrift insolvencies, the FDIC uses the deposit insurance fund, comprised of the (continued...)

There is also a section in the proposal allowing assessments to recover funds expended by the FDIC under this proposal. It reads:

> (1) Recovery of expended funds.—The Corporation shall take steps to recover the amount of funds expended by the Corporation under this section that the Corporation has not otherwise recouped. Such steps shall include 1 or more emergency special assessments on financial companies taking into consideration the following—
>
> (A) The net present value of the appropriated funds expended;
>
> (B) The amount and frequency of assessments to recover the full amount of appropriated funds expended within 60 months from the date of the determination in subsection (b); and
>
> (C) Such other considerations that the Corporation and the Secretary deem appropriate.
>
> (2) Rulemaking.—The Corporation and the Secretary shall issue joint regulations to carry out this subsection.[129]

It appears to contemplate a system similar to the Federal Deposit Insurance system, whereby the companies potentially subject to the FDIC's resolution authority under this proposal would be assessed premiums to fund the resolutions. The text provides no explicit indication of when such a system would be set up or the extent of its coverage, i.e., whether all companies included in the definition of "financial company" would be required; when the assessments would be triggered; or what the rate of the assessment would be.

Clarification of Criminal Provision Regarding Concealing Assets From a Conservator, Receiver, or Liquidating Agent

Section 3 of the proposal amends 18 U.S.C. § 1032 to make the criminal prohibition on concealing assets from a conservator, receiver, or liquidating agent applicable to the FDIC as a conservator or receiver of a company subject to a Systemic Risk Determination.

Miscellaneous Provisions

One provision of the proposal exempts "covered financial company as that term is defined in section 2" of the proposal from coverage by the bankruptcy code; another provision applies the bilateral and clearing organization netting requirements of 12 U.S.C. §§ 4401-4422, to the FDIC's resolution authority under this proposal and that of the Federal Housing Finance Agency .

(...continued)

premiums assessed upon institutions with insured deposits. In the event of multiple bank or thrift failures that exhaust the deposit insurance fund, federal appropriations would be necessary to supplement the deposit insurance fund and protect insured depositors.

[129] *Id.*, § 2(v).

Appendix A. Forms of Banking Organizations

The structure of banks can be complex. Currently, the regulator of a particular activity of a bank or its subsidiary in part depends on the activity of the subsidiary or its charter, as described above. The following flow charts provide simplified representations of various bank structures. In some cases, the umbrella bank and its subsidiaries may have different regulators.

Figure A-1. National Bank

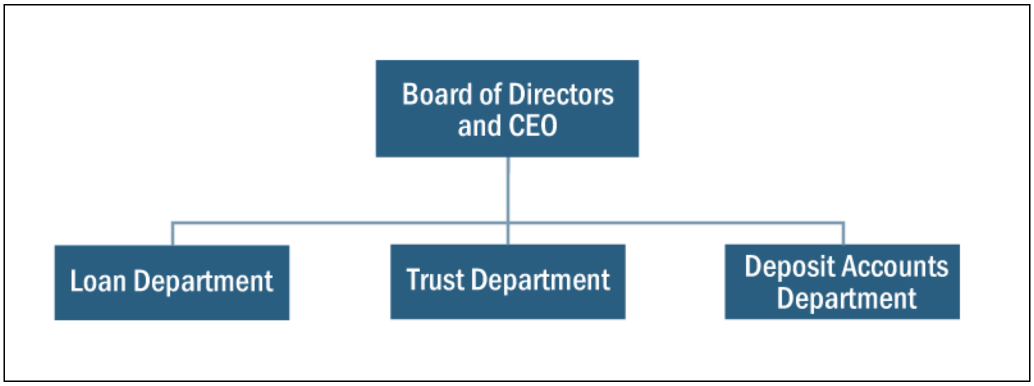


Figure A-2. National Bank and Subsidiaries

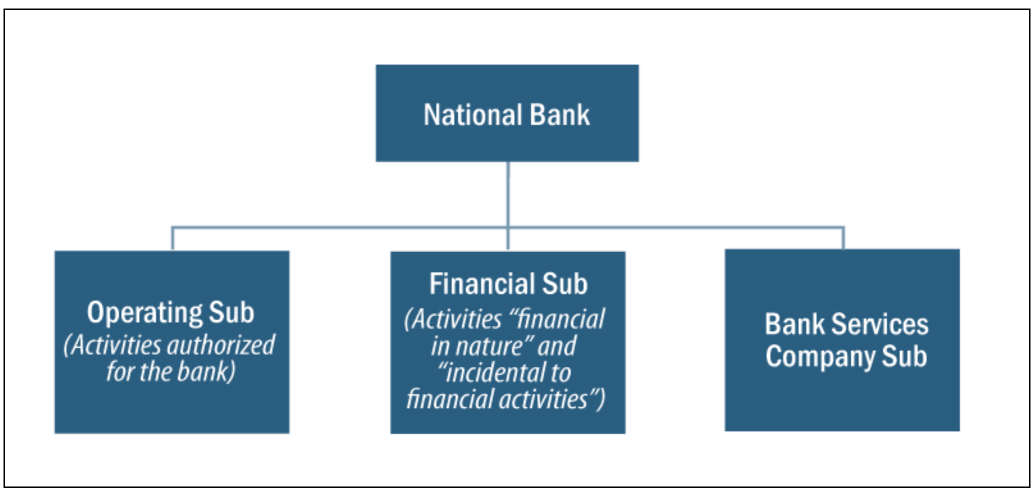


Figure A-3. Bank Holding Company

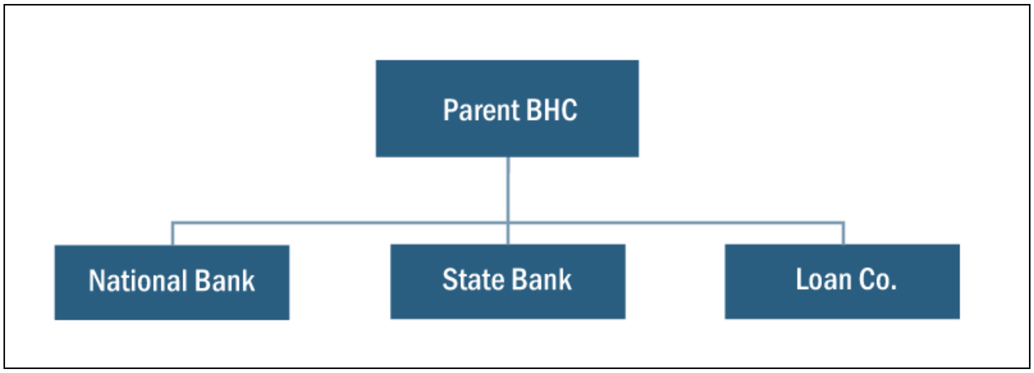
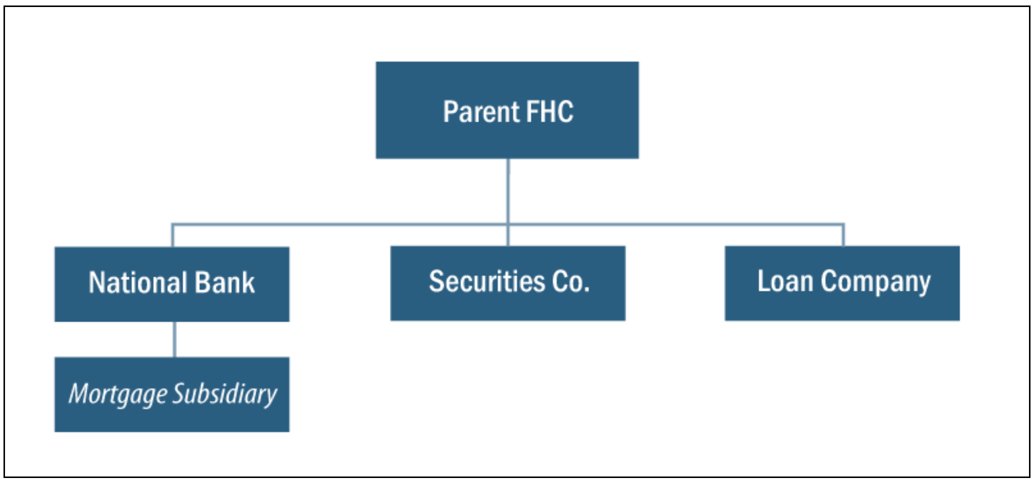


Figure A-4. Financial Holding Company



Appendix B. Activities Considered Financial in Nature Under Section 4(k)(4) of the Bank Holding Company Act, 12 U.S. § 1843(k)(4)

Activities That Are Financial in Nature

For purposes of this subsection, the following activities shall be considered to be financial in nature:

(A) Lending, exchanging, transferring, investing for others, or safeguarding money or securities.

(B) Insuring, guaranteeing, or indemnifying against loss, harm, damage, illness, disability, or death, or providing and issuing annuities, and acting as principal, agent, or broker for purposes of the foregoing, in any State.

(C) Providing financial, investment, or economic advisory services, including advising an investment company (as defined in section 3 of the Investment Company Act of 1940).

(D) Issuing or selling instruments representing interests in pools of assets permissible for a bank to hold directly.

(E) Underwriting, dealing in, or making a market in securities.

(F) Engaging in any activity that the Board has determined, by order or regulation that is in effect on the date of the enactment of the Gramm-Leach-Bliley Act, to be so closely related to banking or managing or controlling banks as to be a proper incident thereto (subject to the same terms and conditions contained in such order or regulation, unless modified by the Board).

(G) Engaging, in the United States, in any activity that—

(i) a bank holding company may engage in outside the United States; and

(ii) the Board has determined, under regulations prescribed or interpretation issued pursuant to subsection (c)(13) (as in effect on the day before the date of the enactment of the Gramm-Leach-Bliley Act) to be usual in connection with the transaction of banking or other financial operations abroad.

(H) Directly or indirectly acquiring or controlling, whether as principal, on behalf of 1 or more entities (including entities, other than a depository institution or subsidiary of a depository institution, that the bank holding company controls), or otherwise, shares, assets, or ownership interests (including debt or equity securities, partnership interests, trust certificates, or other instruments representing ownership) of a company or other entity, whether or not constituting control of such company or entity, engaged in any activity not authorized pursuant to this section if—

(i) the shares, assets, or ownership interests are not acquired or held by a depository institution or subsidiary of a depository institution;

(ii) such shares, assets, or ownership interests are acquired and held by—

(I) a securities affiliate or an affiliate thereof; or

(II) an affiliate of an insurance company described in subparagraph (I)(ii) that provides investment advice to an insurance company and is registered pursuant to the Investment Advisors Act of 1940, or an affiliate of such investment advisor; as part of a bona fide underwriting or merchant or investment banking activity, including investment activities engaged in for the purpose of appreciation and ultimate resale or disposition of the investment;

(iii) such shares, assets, or ownership interests are held for a period of time to enable the sale or disposition thereof on a reasonable basis consistent with the financial viability of the activities described in clause (ii); and

(iv) during the period such shares, assets or ownership interests are held, the bank holding company does not routinely manage or operate such company or entity except as may be necessary or required to obtain a reasonable return on investment upon resale or disposition.

(I) Directly or indirectly acquiring or controlling, whether as principal, on behalf of 1 or more entities (including entities, other than a depository institution or subsidiary of a depository institution, that the bank holding company controls) or otherwise, shares, assets, or ownership interests, trust certificates or other instruments representing ownership) of a company or other entity, whether or not constituting control of such company or entity, engaged in any activity not authorized pursuant to this section if—

(i) the shares, assets, or ownership interests are not acquired or held by a depository institution or a subsidiary of a depository institution;

(ii) such shares, assets, or ownership interests are acquired and held by an insurance company that is predominantly engaged in underwriting life, accident and health, or property and casualty insurance (other that credit-related insurance) or providing and issuing annuities;

(iii) such shares, assets, or ownership interests represent an investment made in the ordinary course of business of such insurance company in accordance with relevant State law governing such investment; and

(iv) during the period such shares, assets, or ownership interests are held, the bank holding company does not routinely manage or operate such company except as may be necessary or required to obtain a reasonable return on investment.

Appendix C. Permissible Non-Banking Activities: 12 C.F.R. § 225.28

List of Permissible Nonbanking Activities

(a) *Closely related nonbanking activities.* The activities listed in paragraph (b) of this section are so closely related to banking or managing or controlling banks as to be a proper incident thereto, and may be engaged in by a bank holding company or its subsidiary in accordance with the requirements of this regulation.

(b) *Activities determined by regulation to be permissible*—(1) *Extending credit and servicing loans.* Making, acquiring, brokering, or servicing loans or other extensions of credit (including factoring, issuing letters of credit and accepting drafts) for the company's account or for the account of others.

(2) *Activities related to extending credit.* Any activity usual in connection with making, acquiring, brokering or servicing loans or other extensions of credit, as determined by the Board. The Board has determined that the following activities are usual in connection with making, acquiring, brokering or servicing loans or other extensions of credit:

(i) *Real estate and personal property appraising.* Performing appraisals of real estate and tangible and intangible personal property, including securities.

(ii) *Arranging commercial real estate equity financing.* Acting as intermediary for the financing of commercial or industrial income-producing real estate by arranging for the transfer of the title, control, and risk of such a real estate project to one or more investors, if the bank holding company and its affiliates do not have an interest in, or participate in managing or developing, a real estate project for which it arranges equity financing, and do not promote or sponsor the development of the property.

(iii) *Check-guaranty services.* Authorizing a subscribing merchant to accept personal checks tendered by the merchant's customers in payment for goods and services, and purchasing from the merchant validly authorized checks that are subsequently dishonored.

(iv) *Collection agency services.* Collecting overdue accounts receivable, either retail or commercial.

(v) *Credit bureau services.* Maintaining information related to the credit history of consumers and providing the information to a credit grantor who is considering a borrower's application for credit or who has extended credit to the borrower.

(vi) *Asset management, servicing, and collection activities.* Engaging under contract with a third party in asset management, servicing, and collection[130] of assets of a type that an insured depository institution may originate and own, if the company does not engage in real property management or real estate brokerage services as part of these services.

[130] Asset management services include acting as agent in the liquidation or sale of loans and collateral for loans, including real estate and other assets acquired through foreclosure or in satisfaction of debts previously contracted.

(vii) *Acquiring debt in default.* Acquiring debt that is in default at the time of acquisition, if the company:

(A) Divests shares or assets securing debt in default that are not permissible investments for bank holding companies, within the time period required for divestiture of property acquired in satisfaction of a debt previously contracted under §225.12(b);[131]

(B) Stands only in the position of a creditor and does not purchase equity of obligors of debt in default (other than equity that may be collateral for such debt); and

(C) Does not acquire debt in default secured by shares of a bank or bank holding company.

(viii) *Real estate settlement servicing.* Providing real estate settlement services.[132]

(3) *Leasing personal or real property.* Leasing personal or real property or acting as agent, broker, or adviser in leasing such property if:

(i) The lease is on a nonoperating basis;[133]

(ii) The initial term of the lease is at least 90 days;

(iii) In the case of leases involving real property:

(A) At the inception of the initial lease, the effect of the transaction will yield a return that will compensate the lessor for not less than the lessor's full investment in the property plus the estimated total cost of financing the property over the term of the lease from rental payments, estimated tax benefits, and the estimated residual value of the property at the expiration of the initial lease; and

(B) The estimated residual value of property for purposes of paragraph (b)(3)(iii)(A) of this section shall not exceed 25 percent of the acquisition cost of the property to the lessor.

(4) *Operating nonbank depository institutions*—(i) *Industrial banking.* Owning, controlling, or operating an industrial bank, Morris Plan bank, or industrial loan company, so long as the institution is not a bank.

(ii) *Operating savings association.* Owning, controlling, or operating a savings association, if the savings association engages only in deposit-taking activities, lending, and other activities that are permissible for bank holding companies under this subpart C.

[131] For this purpose, the divestiture period for property begins on the date that the debt is acquired, regardless of when legal title to the property is acquired.

[132] For purposes of this section, real estate settlement services do not include providing title insurance as principal, agent, or broker.

[133] The requirement that the lease be on a nonoperating basis means that the bank holding company may not, directly or indirectly, engage in operating, servicing, maintaining, or repairing leased property during the lease term. For purposes of the leasing of automobiles, the requirement that the lease be on a nonoperating basis means that the bank holding company may not, directly or indirectly: (1) Provide servicing, repair, or maintenance of the leased vehicle during the lease term; (2) purchase parts and accessories in bulk or for an individual vehicle after the lessee has taken delivery of the vehicle; (3) provide the loan of an automobile during servicing of the leased vehicle; (4) purchaseinsurance for the lessee; or (5) provide for the renewal of the vehicle's license merely as a service to the lessee where the lessee could renew the license without authorization from the lessor. The bank holding company may arrange for a third party to provide these services or products.

(5) *Trust company functions.* Performing functions or activities that may be performed by a trust company (including activities of a fiduciary, agency, or custodial nature), in the manner authorized by federal or state law, so long as the company is not a bank for purposes of section 2(c) of the Bank Holding Company Act.

(6) *Financial and investment advisory activities.* Acting as investment or financial advisor to any person, including (without, in any way, limiting the foregoing):

(i) Serving as investment adviser (as defined in section 2(a)(20) of the Investment Company Act of 1940, 15 U.S.C. 80a–2(a)(20)), to an investment company registered under that act, including sponsoring, organizing, and managing a closed-end investment company;

(ii) Furnishing general economic information and advice, general economic statistical forecasting services, and industry studies;

(iii) Providing advice in connection with mergers, acquisitions, divestitures, investments, joint ventures, leveraged buyouts, recapitalizations, capital structurings, financing transactions and similar transactions, and conducting financial feasibility studies;[134]

(iv) Providing information, statistical forecasting, and advice with respect to any transaction in foreign exchange, swaps, and similar transactions, commodities, and any forward contract, option, future, option on a future, and similar instruments;

(v) Providing educational courses, and instructional materials to consumers on individual financial management matters; and

(vi) Providing tax-planning and tax-preparation services to any person.

(7) *Agency transactional services for customer investments*—(i) *Securities brokerage.* Providing securities brokerage services (including securities clearing and/or securities execution services on an exchange), whether alone or in combination with investment advisory services, and incidental activities (including related securities credit activities and custodial services), if the securities brokerage services are restricted to buying and selling securities solely as agent for the account of customers and do not include securities underwriting or dealing.

(ii) *Riskless principal transactions.* Buying and selling in the secondary market all types of securities on the order of customers as a "riskless principal" to the extent of engaging in a transaction in which the company, after receiving an order to buy (or sell) a security from a customer, purchases (or sells) the security for its own account to offset a contemporaneous sale to (or purchase from) the customer. This does not include:

(A) Selling bank-ineligible securities[135] at the order of a customer that is the issuer of the securities, or selling bank-ineligible securities in any transaction where the company has a contractual agreement to place the securities as agent of the issuer; or

[134] Feasibility studies do not include assisting management with the planning or marketing for a given project or providing general operational or management advice.

[135] A bank-ineligible security is any security that a State member bank is not permitted to underwrite or deal in under 12 U.S.C. 24 and 335.

(B) Acting as a riskless principal in any transaction involving a bank-ineligible security for which the company or any of its affiliates acts as underwriter (during the period of the underwriting or for 30 days thereafter) or dealer.[136]

(iii) *Private placement services.* Acting as agent for the private placement of securities in accordance with the requirements of the Securities Act of 1933 (1933 Act) and the rules of the Securities and Exchange Commission, if the company engaged in the activity does not purchase or repurchase for its own account the securities being placed, or hold in inventory unsold portions of issues of these securities.

(iv) *Futures commission merchant.* Acting as a futures commission merchant (FCM) for unaffiliated persons in the execution, clearance, or execution and clearance of any futures contract and option on a futures contract traded on an exchange in the United States or abroad if:

(A) The activity is conducted through a separately incorporated subsidiary of the bank holding company, which may engage in activities other than FCM activities (including, but not limited to, permissible advisory and trading activities); and

(B) The parent bank holding company does not provide a guarantee or otherwise become liable to the exchange or clearing association other than for those trades conducted by the subsidiary for its own account or for the account of any affiliate.

(v) *Other transactional services.* Providing to customers as agent transactional services with respect to swaps and similar transactions, any transaction described in paragraph (b)(8) of this section, any transaction that is permissible for a state member bank, and any other transaction involving a forward contract, option, futures, option on a futures or similar contract (whether traded on an exchange or not) relating to a commodity that is traded on an exchange.

(8) *Investment transactions as principal*—(i) *Underwriting and dealing in government obligations and money market instruments.* Underwriting and dealing in obligations of the United States, general obligations of states and their political subdivisions, and other obligations that state member banks of the Federal Reserve System may be authorized to underwrite and deal in under 12 U.S.C. 24 and 335, including banker's acceptances and certificates of deposit, under the same limitations as would be applicable if the activity were performed by the bank holding company's subsidiary member banks or its subsidiary nonmember banks as if they were member banks.

(ii) *Investing and trading activities.* Engaging as principal in:

(A) Foreign exchange;

(B) Forward contracts, options, futures, options on futures, swaps, and similar contracts, whether traded on exchanges or not, based on any rate, price, financial asset (including gold,

[136] A company or its affiliates may not enter quotes for specific bank-ineligible securities in any dealer quotation system in connection with the company's riskless principal transactions; except that the company or its affiliates may enter "bid" or "ask" quotations, or publish "offering wanted" or "bid wanted" notices on trading systems other than NASDAQ or an exchange, if the company or its affiliate does not enter price quotations on different sides of the market for a particular security during any two-day period.

silver, platinum, palladium, copper, or any other metal approved by the Board), nonfinancial asset, or group of assets, other than a bank-ineligible security,[137] if:

(*1*) A state member bank is authorized to invest in the asset underlying the contract;

(*2*) The contract requires cash settlement;

(*3*) The contract allows for assignment, termination, or offset prior to delivery or expiration, and the company—

(*i*) Makes every reasonable effort to avoid taking or making delivery of the asset underlying the contract; or

(*ii*) Receives and instantaneously transfers title to the underlying asset, by operation of contract and without taking or making physical delivery of the asset; or

(*4*) The contract does not allow for assignment, termination, or offset prior to delivery or expiration and is based on an asset for which futures contracts or options on futures contracts have been approved for trading on a U.S. contract market by the Commodity Futures Trading Commission, and the company—

(*i*) Makes every reasonable effort to avoid taking or making delivery of the asset underlying the contract; or

(*ii*) Receives and instantaneously transfers title to the underlying asset, by operation of contract and without taking or making physical delivery of the asset.

(C) Forward contracts, options,[138] futures, options on futures, swaps, and similar contracts, whether traded on exchanges or not, based on an index of a rate, a price, or the value of any financial asset, nonfinancial asset, or group of assets, if the contract requires cash settlement.

(iii) *Buying and selling bullion, and related activities.* Buying, selling and storing bars, rounds, bullion, and coins of gold, silver, platinum, palladium, copper, and any other metal approved by the Board, for the company's own account and the account of others, and providing incidental services such as arranging for storage, safe custody, assaying, and shipment.

(9) *Management consulting and counseling activities*—(i) *Management consulting.* (A) Providing management consulting advice:[139]

[137] A bank-ineligible security is any security that a state member bank is not permitted to underwrite or deal in under 12 U.S.C. 24 and 335.

[138] This reference does not include acting as a dealer in options based on indices of bank-ineligible securities when the options are traded on securities exchanges. These options are securities for purposes of the federal securities laws and bank-ineligible securities for purposes of section 20 of the Glass-Steagall Act, 12 U.S.C. 337. Similarly, this reference does not include acting as a dealer in any other instrument that is a bank-ineligible security for purposes of section 20. A bank holding company may deal in these instruments in accordance with the Board's orders on dealing in bank-ineligible securities.

[139] In performing this activity, bank holding companies are not authorized to perform tasks or operations or provide services to client institutions either on a daily or continuing basis, except as necessary to instruct the client institution on how to perform such services for itself. See also the Board's interpretation of bank management consulting advice (12 CFR 225.131).

(*1*) On any matter to unaffiliated depository institutions, including commercial banks, savings and loan associations, savings banks, credit unions, industrial banks, Morris Plan banks, cooperative banks, industrial loan companies, trust companies, and branches or agencies of foreign banks;

(*2*) On any financial, economic, accounting, or audit matter to any other company.

(B) A company conducting management consulting activities under this subparagraph and any affiliate of such company may not:

(*1*) Own or control, directly or indirectly, more than 5 percent of the voting securities of the client institution; and

(*2*) Allow a management official, as defined in 12 CFR 212.2(h), of the company or any of its affiliates to serve as a management official of the client institution, except where such interlocking relationship is permitted pursuant to an exemption granted under 12 CFR 212.4(b) or otherwise permitted by the Board.

(C) A company conducting management consulting activities may provide management consulting services to customers not described in paragraph (b)(9)(i)(A)(*1*) of this section or regarding matters not described in paragraph (b)(9)(i)(A)(*2*) of this section, if the total annual revenue derived from those management consulting services does not exceed 30 percent of the company's total annual revenue derived from management consulting activities.

(ii) *Employee benefits consulting services.* Providing consulting services to employee benefit, compensation and insurance plans, including designing plans, assisting in the implementation of plans, providing administrative services to plans, and developing employee communication programs for plans.

(iii) *Career counseling services.* Providing career counseling services to:

(A) A financial organization[140] and individuals currently employed by, or recently displaced from, a financial organization;

(B) Individuals who are seeking employment at a financial organization; and

(C) Individuals who are currently employed in or who seek positions in the finance, accounting, and audit departments of any company.

(10) *Support services*—(i) *Courier services.* Providing courier services for:

(A) Checks, commercial papers, documents, and written instruments (excluding currency or bearer-type negotiable instruments) that are exchanged among banks and financial institutions; and

(B) Audit and accounting media of a banking or financial nature and other business records and documents used in processing such media.[141]

[140] *Financial organization* refers to insured depository institution holding companies and their subsidiaries, other than nonbanking affiliates of diversified savings and loan holding companies that engage in activities not permissible under section 4(c)(8) of the Bank Holding Company Act (12 U.S.C. 1842(c)(8)).

[141] See also the Board's interpretation on courier activities (12 CFR 225.129), which sets forth conditions for bank (continued...)

(ii) *Printing and selling MICR-encoded items.* Printing and selling checks and related documents, including corporate image checks, cash tickets, voucher checks, deposit slips, savings withdrawal packages, and other forms that require Magnetic Ink Character Recognition (MICR) encoding.

(11) *Insurance agency and underwriting*—(i) *Credit insurance.* Acting as principal, agent, or broker for insurance (including home mortgage redemption insurance) that is:

(A) Directly related to an extension of credit by the bank holding company or any of its subsidiaries; and

(B) Limited to ensuring the repayment of the outstanding balance due on the extension of credit[142] in the event of the death, disability, or involuntary unemployment of the debtor.

(ii) *Finance company subsidiary.* Acting as agent or broker for insurance directly related to an extension of credit by a finance company[143] that is a subsidiary of a bank holding company, if:

(A) The insurance is limited to ensuring repayment of the outstanding balance on such extension of credit in the event of loss or damage to any property used as collateral for the extension of credit; and

(B) The extension of credit is not more than $10,000, or $25,000 if it is to finance the purchase of a residential manufactured home[144] and the credit is secured by the home; and

(C) The applicant commits to notify borrowers in writing that:

(*1*) They are not required to purchase such insurance from the applicant;

(*2*) Such insurance does not insure any interest of the borrower in the collateral; and

(*3*) The applicant will accept more comprehensive property insurance in place of such single-interest insurance.

(iii) *Insurance in small towns.* Engaging in any insurance agency activity in a place where the bank holding company or a subsidiary of the bank holding company has a lending office and that:

(A) Has a population not exceeding 5,000 (as shown in the preceding decennial census); or

(B) Has inadequate insurance agency facilities, as determined by the Board, after notice and opportunity for hearing.

(...continued)

holding company entry into the activity.

[142] *Extension of credit* includes direct loans to borrowers, loans purchased from other lenders, and leases of real or personal property so long as the leases are nonoperating and full-payout leases that meet the requirements of paragraph (b)(3) of this section.

[143] *Finance company* includes all non-deposit-taking financial institutions that engage in a significant degree of consumer lending (excluding lending secured by first mortgages) and all financial institutions specifically defined by individual states as finance companies and that engage in a significant degree of consumer lending.

[144] These limitations increase at the end of each calendar year, beginning with 1982, by the percentage increase in the Consumer Price Index for Urban Wage Earners and Clerical Workers published by the Bureau of Labor Statistics.

(iv) *Insurance-agency activities conducted on May 1, 1982.* Engaging in any specific insurance-agency activity[145] if the bank holding company, or subsidiary conducting the specific activity, conducted such activity on May 1, 1982, or received Board approval to conduct such activity on or before May 1, 1982.[146] A bank holding company or subsidiary engaging in a specific insurance agency activity under this clause may:

(A) Engage in such specific insurance agency activity only at locations:

(*1*) In the state in which the bank holding company has its principal place of business (as defined in 12 U.S.C. 1842(d));

(*2*) In any state or states immediately adjacent to such state; and

(*3*) In any state in which the specific insurance-agency activity was conducted (or was approved to be conducted) by such bank holding company or subsidiary thereof or by any other subsidiary of such bank holding company on May 1, 1982; and

(B) Provide other insurance coverages that may become available after May 1, 1982, so long as those coverages insure against the types of risks as (or are otherwise functionally equivalent to) coverages sold or approved to be sold on May 1, 1982, by the bank holding company or subsidiary.

(v) *Supervision of retail insurance agents.* Supervising on behalf of insurance underwriters the activities of retail insurance agents who sell:

(A) Fidelity insurance and property and casualty insurance on the real and personal property used in the operations of the bank holding company or its subsidiaries; and

(B) Group insurance that protects the employees of the bank holding company or its subsidiaries.

(vi) *Small bank holding companies.* Engaging in any insurance-agency activity if the bank holding company has total consolidated assets of $50 million or less. A bank holding company performing insurance-agency activities under this paragraph may not engage in the sale of life insurance or annuities except as provided in paragraphs (b)(11) (i) and (iii) of this section, and it may not continue to engage in insurance-agency activities pursuant to this provision more than 90 days after the end of the quarterly reporting period in which total assets of the holding company and its subsidiaries exceed $50 million.

(vii) *Insurance-agency activities conducted before 1971.* Engaging in any insurance-agency activity performed at any location in the United States directly or indirectly by a bank holding company that was engaged in insurance-agency activities prior to January 1, 1971, as a consequence of approval by the Board prior to January 1, 1971.

[145] Nothing contained in this provision shall preclude a bank holding company subsidiary that is authorized to engage in a specific insurance-agency activity under this clause from continuing to engage in the particular activity after merger with an affiliate, if the merger is for legitimate business purposes and prior notice has been provided to the Board.

[146] For the purposes of this paragraph, activities engaged in on May 1, 1982, include activities carried on subsequently as the result of an application to engage in such activities pending before the Board on May 1, 1982, and approved subsequently by the Board or as the result of the acquisition by such company pursuant to a binding written contract entered into on or before May 1, 1982, of another company engaged in such activities at the time of the acquisition.

(12) *Community development activities*—(i) *Financing and investment activities.* Making equity and debt investments in corporations or projects designed primarily to promote community welfare, such as the economic rehabilitation and development of low-income areas by providing housing, services, or jobs for residents.

(ii) *Advisory activities.* Providing advisory and related services for programs designed primarily to promote community welfare.

(13) *Money orders, savings bonds, and traveler's checks.* The issuance and sale at retail of money orders and similar consumer-type payment instruments; the sale of U.S. savings bonds; and the issuance and sale of traveler's checks.

(14) *Data processing.* (i) Providing data processing, data storage and data transmission services, facilities (including data processing, data storage and data transmission hardware, software, documentation, or operating personnel), databases, advice, and access to such services, facilities, or data-bases by any technological means, if:

(A) The data to be processed, stored or furnished are financial, banking or economic; and

(B) The hardware provided in connection therewith is offered only in conjunction with software designed and marketed for the processing, storage and transmission of financial, banking, or economic data, and where the general purpose hardware does not constitute more than 30 percent of the cost of any packaged offering.

(ii) A company conducting data processing, data storage, and data transmission activities may conduct data processing, data storage, and data transmission activities not described in paragraph (b)(14)(i) of this section if the total annual revenue derived from those activities does not exceed 49 percent of the company's total annual revenues derived from data processing, data storage and data transmission activities.

[Reg. Y, 62 FR 9329, Feb. 28, 1997, as amended at 68 FR 39810, July 3, 2003; 68 FR 41901, July 16, 2003; 68 FR 68499, Dec. 9, 2003, footnotes omitted.]

Appendix D. Activities Permissible for Financial Holding Companies Under 12 C.F.R. § 225.86

Activities That Are Financial in Nature or Incidental to a Financial Activity

(a) *Activities determined to be closely related to banking.* (1) Any activity that the Board had determined by regulation prior to November 12, 1999, to be so closely related to banking as to be a proper incident thereto, subject to the terms and conditions contained in this part, unless modified by the Board. These activities are listed in §225.28.

(2) Any activity that the Board had determined by an order that was in effect on November 12, 1999, to be so closely related to banking as to be a proper incident thereto, subject to the terms and conditions contained in this part and those in the authorizing orders. These activities are:

(i) Providing administrative and other services to mutual funds (*Societe Generale,* 84 Federal Reserve Bulletin 680 (1998));

(ii) Owning shares of a securities exchange (*J.P. Morgan & Co, Inc., and UBS AG,* 86 Federal Reserve Bulletin 61 (2000));

(iii) Acting as a certification authority for digital signatures and authenticating the identity of persons conducting financial and nonfinancial transactions (*Bayerische Hypo- und Vereinsbank AG, et al.,* 86 Federal Reserve Bulletin 56 (2000));

(iv) Providing employment histories to third parties for use in making credit decisions and to depository institutions and their affiliates for use in the ordinary course of business (*Norwest Corporation,* 81 Federal Reserve Bulletin 732 (1995));

(v) Check cashing and wire transmission services (*Midland Bank, PLC*, 76 Federal Reserve Bulletin 860 (1990) (check cashing); *Norwest Corporation*, 81 Federal Reserve Bulletin 1130 (1995) (money transmission));

(vi) In connection with offering banking services, providing notary public services, selling postage stamps and postage-paid envelopes, providing vehicle registration services, and selling public transportation tickets and tokens (*Popular, Inc.*, 84 Federal Reserve Bulletin 481 (1998)); and

(vii) Real estate title abstracting (*The First National Company,* 81 Federal Reserve Bulletin 805 (1995)).

(b) *Activities determined to be usual in connection with the transaction of banking abroad.* Any activity that the Board had determined by regulation in effect on November 11, 1999, to be usual in connection with the transaction of banking or other financial operations abroad (*see* §211.5(d) of this chapter), subject to the terms and conditions in part 211 and Board interpretations in effect on that date regarding the scope and conduct of the activity. In addition to the activities listed in paragraphs (a) and (c) of this section, these activities are:

(1) Providing management consulting services, including to any person with respect to nonfinancial matters, so long as the management consulting services are advisory and do not allow the financial holding company to control the person to which the services are provided;

(2) Operating a travel agency in connection with financial services offered by the financial holding company or others; and

(3) Organizing, sponsoring, and managing a mutual fund, so long as:

(i) The fund does not exercise managerial control over the entities in which the fund invests; and

(ii) The financial holding company reduces its ownership in the fund, if any, to less than 25 percent of the equity of the fund within one year of sponsoring the fund or such additional period as the Board permits.

(c) *Activities permitted under section 4(k)(4) of the BHC Act* (12 U.S.C. 1843(k)(4)). Any activity defined to be financial in nature under sections 4(k)(4)(A) through (E), (H) and (I) of the BHC Act (12 U.S.C. 1843(k)(4)(A) through (E), (H) and (I)).

(d) *Activities determined to be financial in nature or incidental to financial activities by the Board*—(1) *Acting as a finder*—Acting as a finder in bringing together one or more buyers and sellers of any product or service for transactions that the parties themselves negotiate and consummate.

(i) *What is the scope of finder activities?* Acting as a finder includes providing any or all of the following services through any means—

(A) Identifying potential parties, making inquiries as to interest, introducing and referring potential parties to each other, and arranging contacts between and meetings of interested parties;

(B) Conveying between interested parties expressions of interest, bids, offers, orders and confirmations relating to a transaction; and

(C) Transmitting information concerning products and services to potential parties in connection with the activities described in paragraphs (d)(1)(i)(A) and (B) of this section.

(ii) *What are some examples of finder services?* The following are examples of the services that may be provided by a finder when done in accordance with paragraphs (d)(1)(iii) and (iv) of this section. These examples are not exclusive.

(A) Hosting an electronic marketplace on the financial holding company's Internet web site by providing hypertext or similar links to the web sites of third party buyers or sellers.

(B) Hosting on the financial holding company's servers the Internet web site of—

(*1*) A buyer (or seller) that provides information concerning the buyer (or seller) and the products or services it seeks to buy (or sell) and allows sellers (or buyers) to submit expressions of interest, bids, offers, orders and confirmations relating to such products or services; or

(*2*) A government or government agency that provides information concerning the services or benefits made available by the government or government agency, assists persons in completing applications to receive such services or benefits from the government or agency, and allows persons to transmit their applications for services or benefits to the government or agency.

(C) Operating an Internet web site that allows multiple buyers and sellers to exchange information concerning the products and services that they are willing to purchase or sell, locate potential counterparties for transactions, aggregate orders for goods or services with those made by other parties, and enter into transactions between themselves.

(D) Operating a telephone call center that provides permissible finder services.

(iii) *What limitations are applicable to a financial holding company acting as a finder?* (A) A finder may act only as an intermediary between a buyer and a seller.

(B) A finder may not bind any buyer or seller to the terms of a specific transaction or negotiate the terms of a specific transaction on behalf of a buyer or seller, except that a finder may—

(*1*) Arrange for buyers to receive preferred terms from sellers so long as the terms are not negotiated as part of any individual transaction, are provided generally to customers or broad categories of customers, and are made available by the seller (and not by the financial holding company); and

(*2*) Establish rules of general applicability governing the use and operation of the finder service, including rules that—

(*i*) Govern the submission of bids and offers by buyers and sellers that use the finder service and the circumstances under which the finder service will match bids and offers submitted by buyers and sellers; and

(*ii*) Govern the manner in which buyers and sellers may bind themselves to the terms of a specific transaction.

(C) A finder may not—

(*1*) Take title to or acquire or hold an ownership interest in any product or service offered or sold through the finder service;

(*2*) Provide distribution services for physical products or services offered or sold through the finder service;

(*3*) Own or operate any real or personal property that is used for the purpose of manufacturing, storing, transporting, or assembling physical products offered or sold by third parties; or

(*4*) Own or operate any real or personal property that serves as a physical location for the physical purchase, sale or distribution of products or services offered or sold by third parties.

(D) A finder may not engage in any activity that would require the company to register or obtain a license as a real estate agent or broker under applicable law.

(iv) *What disclosures are required?* A finder must distinguish the products and services offered by the financial holding company from those offered by a third party through the finder service.

(2) [Reserved]

(e) *Activities permitted under section 4(k)(5) of the Bank Holding Company Act (12 U.S.C. 1843(k)(5)).* (1) The following types of activities are financial in nature or incidental to a financial activity when conducted pursuant to a determination by the Board under paragraph (e)(2) of this section:

(i) Lending, exchanging, transferring, investing for others, or safeguarding financial assets other than money or securities;

(ii) Providing any device or other instrumentality for transferring money or other financial assets; and

(iii) Arranging, effecting, or facilitating financial transactions for the account of third parties.

(2) *Review of specific activities*—(i) *Is a specific request required?* A financial holding company that wishes to engage on the basis of paragraph (e)(1) of this section in an activity that is not otherwise permissible for a financial holding company must obtain a determination from the Board that the activity is permitted under paragraph (e)(1).

(ii) *Consultation with the Secretary of the Treasury.* After receiving a request under this section, the Board will provide the Secretary of the Treasury with a copy of the request and consult with the Secretary in accordance with section 4(k)(2)(A) of the Bank Holding Company Act (12 U.S.C. 1843(k)(2)(A)).

(iii) *Board action on requests.* After consultation with the Secretary, the Board will promptly make a written determination regarding whether the specific activity described in the request is included in an activity category listed in paragraph (e)(1) of this section and is therefore either financial in nature or incidental to a financial activity.

(3) *What factors will the Board consider?* In evaluating a request made under this section, the Board will take into account the factors listed in section 4(k)(3) of the BHC Act (12 U.S.C. 1843(k)(3)) that it must consider when determining whether an activity is financial in nature or incidental to a financial activity.

(4) *What information must the request contain?* Any request by a financial holding company under this section must be in writing and must:

(i) Identify and define the activity for which the determination is sought, specifically describing what the activity would involve and how the activity would be conducted; and

(ii) Provide information supporting the requested determination, including information regarding how the proposed activity falls into one of the categories listed in paragraph (e)(1) of this section, and any other information required by the Board concerning the proposed activity.

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