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## FDIC Issues Interim Rule for its Temporary Liquidity Guarantee Program — Short Comment Period Commences

As described in our earlier Client Alert, on October 14, 2008 the FDIC adopted the Temporary Liquidity Guarantee Program. On October 23, 2008 the FDIC issued its interim rule for the program and requested comment on the rule. This alert fleshes out additional details regarding this program that are addressed by the interim rule but were not included in the earlier FDIC press releases. We encourage you to consider commenting on any aspect of the rule that you believe needs reformation. Comments are due no later than 15 days after the interim rule is published in the *Federal Register*. Accordingly, comments may be due as early as November 7, 2008.

The two elements of the program are the senior unsecured debt guarantee and the additional insurance on noninterest-bearing transaction deposit accounts. This Client Alert summarizes the interim rule and focuses on the additional details and clarifications presented by the rule. The two most significant developments presented by the interim rule both relate to the debt guarantee program.

First, the interim rule clarifies that the issuer (or borrower) is the party subject to the higher assessment for having its debt guaranteed, rather than the holder (or lender) of that debt. Given this clarification, all insured depository institutions that have recently been purchasers of federal funds will need to determine, on or before November 12, 2008, whether they will require the FDIC's guarantee of those

funds (as well as any other unsecured debt) in order to continue to have those resources available to them for the following 7½ months (albeit at a higher cost of funds) or whether they believe that their financial strength will keep their federal funds pipeline open without the guarantee, and thereby reduce their cost of funds.

Second, the interim rule provides a mechanism whereby a participating entity can elect to issue long-term (maturing after June 30, 2012), nonguaranteed debt, but only by paying a fee of 37.5 basis points of the annual amount of that debt. Although this fee is nonrefundable, it can be applied against amounts otherwise payable for the issuance of guaranteed debt under this program.

### General Terms

**Eligible entities** include:

- (1) insured depository institutions;
- (2) bank holding companies that are organized under the laws of any state or the District of Columbia, if they have at least one chartered and operating depository institution within their holding company structure;
- (3) savings and loan holding companies that are organized under the laws of any state or the District of Columbia and either engage only in activities that are permissible for financial holding companies or

have at least one depository institution subsidiary that had an application to engage in nonbanking activities pending on October 13, 2008, if they have at least one chartered and operating depository institution within their holding company structure.

In addition, other affiliates of depository institutions may be treated as eligible entities by the FDIC after consultation with the appropriate federal banking agency.

**Participating entity** means for the relevant periods after November 13, 2008 an eligible entity that has not opted out of the debt guarantee program, the transaction account guarantee program or both.

#### Debt Guarantee Program

For purposes of the debt guarantee program:

**Senior unsecured debt** means unsecured borrowing that:

- is evidenced by a written agreement;
- has a specified and fixed principal amount to be paid in full on demand or on a certain date;
- is noncontingent; and
- is not, by its terms, subordinated to any other liability.

Senior unsecured debt includes, for example, federal funds purchased, promissory notes, commercial paper, unsubordinated unsecured notes, certificates of deposit standing to the credit of a bank, bank deposits in an international banking facility (IBF) of a depository institution, and Eurodollar deposits standing to the credit of a bank. (For this purpose, "bank" means an insured depository institution or a depository institution regulated by a foreign bank supervisory agency.) Senior unsecured

debt may be denominated in foreign currency.

Senior unsecured debt *excludes*, for example, obligations from guarantees or other contingent liabilities, derivatives, derivative-linked products, debt paired with any other security, convertible debt, capital notes, the unsecured portion of otherwise secured debt, negotiable certificates of deposit, and deposits in foreign currency and Eurodollar deposits that represent funds swept from individual, partnership or corporate accounts held at depository institutions. Also excluded are loans to affiliates, including parents and subsidiaries, and institution-affiliated parties.

**Newly issued senior unsecured debt** means senior unsecured debt issued by a participating entity on or after October 14, 2008 and on or before June 30, 2009.

**FDIC-guaranteed debt** means newly issued senior unsecured debt that meets the requirements to be guaranteed under the debt guarantee program and is clearly identified as "guaranteed by the FDIC."

**The guarantee and time limitations.** Under the debt guarantee program, the FDIC guarantees payment of the unpaid principal and contract interest of all FDIC-guaranteed debt issued by the participating entity during the period from October 14, 2008 through June 30, 2009, against the failure of a participating depository institution or the bankruptcy of any other participating entity. For FDIC-guaranteed debt issued on or before June 30, 2009, the FDIC's guarantee will terminate on the earlier of the maturity of the debt or June 30, 2012.

**Guarantee limit.** The maximum amount of debt to be issued under the guarantee is generally limited to 125 percent of the par value of the participating entity's senior unsecured debt,

excluding debt extended to affiliates or institution-affiliated parties, outstanding as of September 30, 2008, that was scheduled to mature on or before June 30, 2009. The FDIC may make exceptions to this guarantee limit and allow a participating entity to exceed the 125 percent guarantee limit, restrict a participating entity to less than 125 percent, or impose other limits or requirements. If a participating entity had no or little senior unsecured debt on September 30, 2008, the entity may seek to have some amount of debt covered by the debt guarantee program. The FDIC, after consultation with the appropriate federal banking agency, will decide whether, and to what extent, such requests will be granted on a case-by-case basis.

If a participating entity issues debt identified as "guaranteed by the FDIC" in excess of its maximum amount, it will become subject to assessment increases.

**Calculation and reporting.** Each participating entity is to calculate the amount of its senior unsecured debt outstanding as of September 30, 2008, excluding debt extended to affiliates, that was scheduled to mature on or before June 30, 2009, using the definitions described in this regulation. Each participating entity will be required to report the calculated amount to the FDIC, even if such amount is zero, in an approved format via *FDICconnect* no later than November 12, 2008.

Debt cannot be issued and identified as guaranteed by the FDIC if, among other things, (1) the proceeds are used to prepay debt that is not FDIC guaranteed, (2) the participating entity exceeds its guarantee limit or (3) the debt is extended to an affiliate, an insider of the participating entity or an insider of an affiliate without FDIC approval of the guarantee.

Participating entities will not be able to select which newly issued senior

unsecured debt is guaranteed debt. All senior unsecured debt issued by a participating entity up to the guarantee limit will become guaranteed debt as and when issued, except for long-term nonguaranteed debt issued pursuant to the following paragraph.

**Long-term nonguaranteed debt option.** On or before 11:59 p.m., Eastern Standard Time, November 12, 2008, a participating entity may also notify the FDIC that it has elected to issue nonguaranteed debt with maturities beyond June 30, 2012, at any time, in any amount and without regard to the guarantee limit. By making this election, the participating entity agrees to pay to the FDIC a nonrefundable fee described below.

#### **Transaction Account Guarantee Program**

In addition to the coverage afforded to depositors under existing law (generally \$250,000 per depositor through December 31, 2009), a depositor's funds in a noninterest-bearing transaction account maintained at a participating depository institution are insured in full from October 14, 2008 through December 31, 2009. A noninterest-bearing transaction account means a transaction account (as defined in 12 C.F.R. 204.2) that:

- is maintained at a depository institution;
- with respect to which interest is neither accrued nor paid; and
- on which the depository institution does not reserve the right to require advance notice of an intended withdrawal.

A noninterest-bearing transaction account does not include, for example, a negotiable order of withdrawal (NOW) account or money market deposit account (MMDA).

In determining whether funds are in a noninterest-bearing transaction, the FDIC will apply its normal rules and procedures for determining account balances at a failed depository institution. Under these procedures, funds may be swept or transferred from a noninterest-bearing transaction account to another type of deposit or nondeposit account. Unless the funds are in a noninterest-bearing transaction account after the completion of a sweep, the funds will not be guaranteed under the transaction account guarantee program. But if the funds are swept from a noninterest-bearing transaction account to a noninterest-bearing savings deposit account, the FDIC will treat the swept funds as being in a noninterest-bearing transaction account, and those funds are guaranteed.

#### **Participation, Opt-out and Disclosures**

From October 14, 2008 through November 12, 2008 each eligible entity is a participating entity in both the debt guarantee program and the transaction account guarantee program, unless the entity opts out. No later than 11:59 p.m., Eastern Standard Time, November 12, 2008, each eligible entity must inform the FDIC if it desires to opt out of the debt guarantee program or the transaction account guarantee program, or both. Failure to opt out by that time constitutes a decision to continue in the program after that date. The choice to opt out, once made, is irrevocable.

All eligible entities within a U.S. bank holding company group or U.S. savings and loan holding company group must make the same decision regarding continued participation in each guarantee program; failure to do so constitutes an opt-out by all members of the group.

**Procedures for Opting Out.** The FDIC will provide procedures for opting out using the FDIC's secure e-business

website, *FDICconnect*. Entities that are not depository institutions will select and use an affiliated depository institution to submit their opt-out election and to make any assessment payments required under the temporary liquidity guarantee program.

**Disclosures Regarding Participation.** The FDIC will publish on its website a list of the eligible entities that have opted out of the debt guarantee program or the transaction account guarantee program.

**Debt Guarantee Program.** Each entity participating in the debt guarantee program must clearly identify, in writing and in a commercially reasonable manner, to any interested lender or creditor whether the newly issued debt it is offering is guaranteed or not.

**Transaction Account Guarantee Program.** Each eligible entity that is a depository institution must post a prominent notice in the lobby of its main office and each branch stating whether or not the entity is participating in the transaction account guarantee program. If the entity is participating, the notice must also state that funds held in noninterest-bearing transaction accounts at the entity are insured in full by the FDIC. Furthermore, if the institution uses sweep arrangements or takes other actions that result in funds being transferred or reclassified to an interest-bearing account or nontransaction account, the institution must disclose those actions to the affected customers and clearly advise them, in writing, that such actions will void the FDIC's guarantee.

#### **Assessments**

**Debt Guarantee Program.** Any participating entity that issued guaranteed debt during the period from October 14, 2008 through November 12, 2008 that was still outstanding on November 12, 2008 is required to notify the FDIC of that issuance by December 1, 2008,

and the participating entity must certify that the issuances outstanding did not exceed the guarantee limit.

Any participating entity that issues guaranteed debt after November 12, 2008 must notify the FDIC of that issuance and the participating entity is required to certify that the issuance of guaranteed debt does not exceed the guarantee limit as set forth in section 370.3.

Beginning on November 13, 2008, any participating entity will be charged assessments as follows:

*Amount of assessments for debt within the guarantee limit.* The amount of assessment will be determined by multiplying the amount of eligible guaranteed debt times the term of the debt times an annualized 75 basis points. If the debt matures after June 30, 2012, then June 30, 2012 will be used as the maturity date. A participating entity's assessment will not be reduced if guaranteed debt is retired before its scheduled maturity date.

*Increased assessments for debt exceeding the guarantee limit.* Any par-

ticipating entity that issues guaranteed debt represented as being "guaranteed by the FDIC" that exceeds its guarantee limit will have its assessment rate for all outstanding guaranteed debt increased to 150 basis points. In addition, that entity may also be subject to enforcement action, including civil money penalties.

*Long-term nonguaranteed debt fee.* Each participating entity that elects to issue long-term nonguaranteed debt must pay the FDIC a nonrefundable fee equal to 37.5 basis points times the amount of the entity's senior unsecured debt (other than debt owed to affiliates) with a maturity date on or before June 30, 2009, outstanding as of September 30, 2008. This fee will be collected in six equal monthly installments. An entity electing this option will also be billed as it issues guaranteed debt under the debt guarantee program, and the amounts paid as a nonrefundable fee will be applied to offset these bills until the nonrefundable fee is exhausted. Thereafter, the entity will have to pay additional assessments on guaranteed debt as it issues the debt.

**Transaction Account Guarantee Program.** From November 13, 2008 to December 31, 2009, any participating entity must pay an annualized 10 basis point assessment on any noninterest-bearing transaction accounts exceeding the existing deposit insurance limit of \$250,000, as reported on its quarterly Call Report or Thrift Financial Report. This assessment is in addition to an institution's risk-based assessment imposed by 12 C.F.R. Part 327.

### Oversight

All participating entities availing themselves of the temporary liquidity guarantee program are subject to the FDIC's oversight regarding compliance with the terms of the temporary liquidity guarantee program. Likewise, by issuing guaranteed debt, all participating entities are subject to the FDIC's authority to determine compliance with the requirements of the temporary liquidity guarantee program for the duration of that program.