



## Funding Transactions under the FDIC's Temporary Guarantee Liquidity Program's Debt Guarantee Program

On October 14, 2008, the Federal Deposit Insurance Corporation (FDIC) announced the creation of a new program, the Temporary Liquidity Guarantee Program (TLGP), designed, together with Treasury's Capital Purchase Program and the Federal Reserve's enhanced Commercial Paper Funding Facility, to unfreeze credit markets. Through the TLGP, the FDIC provides insurance to previously uninsured amounts in non-interest bearing transaction deposit accounts and guarantees certain newly-issued senior unsecured debt. Below, we discuss the debt guarantee program.

### Background

Under the TLGP's debt guarantee program (DGP or the Program), newly issued senior unsecured debt issued on or before June 30, 2009 (or October 31, 2009, as described below for the extended DGP) will be fully insured in the event the issuing institution subsequently fails, or its holding company files for bankruptcy. The debt included in the Program includes all newly issued unsecured senior debt, including: promissory notes, commercial paper, inter-bank funding, and any unsecured portion of secured debt. The aggregate newly-issued senior unsecured guaranteed debt a participant may have outstanding may not exceed the issuance cap for that participant. The issuance cap, described in more detail below, is 125% of that participant's outstanding debt on September 30, 2008 that was scheduled to mature on or before June 30, 2009. The guarantee of any newly issued debt will extend to the Program's expiration date, even if the maturity of the debt is after that date. The estimated amount of eligible institution qualifying senior unsecured debt outstanding as of September 30, 2008 is \$1.4 trillion.

As described under "Payment of Claims" below, the FDIC guarantee covers timely payment of interest and principal upon an uncured payment default. The guaranteed debt is backed by the full faith and credit of the United States and has a 20% risk weighting.

The FDIC has announced two amendments to the DGP. On February 27, 2009, the Program was extended to provide a guarantee for an additional category of senior unsecured debt—mandatory convertible debt. On March 17, 2009 the Program was expanded to extend the expiration of the guarantee, extend the last date on which guaranteed debt could be offered and expand the ability of participants to issue non-guaranteed debt. Each of these is discussed in more detail below. In each case, the amendments apply only to those entities that are already participating entities in the Program.

By all accounts the Program has been a success. During the March 17, 2009 FDIC Board meeting, Chairman Bair noted that two-thirds of all public debt issued by banking organizations between October 14, 2008 and March 4, 2009 and maturing on or before June 30, 2012 has been FDIC guaranteed. There have been market improvements as well. In mid-October 2008 the three-month LIBOR spread over Treasuries had risen to 4.57%.

By March 16, 2009 this spread had come down to 1.09%, a dramatic improvement, but still short of the historical spread of approximately 40 basis points.

### Eligibility and Participation

Eligible entities were automatically included in the Program, and the FDIC established December 5, 2008 as an opt-out date. Institutions that are “eligible entities” include (1) FDIC insured depository institutions, (2) U.S. bank holding companies and financial holding companies with at least one operating insured depository institution subsidiary and (3) U.S. savings and loan holding companies, with at least one operating insured depository institution subsidiary, that either engage only in activities that are permissible for financial holding companies to conduct under section 4(k) of the Bank Holding Company Act of 1956 (BHCA) or had at least one insured depository subsidiary that was the subject of an application under section 4(c)(8) of the BHCA pending on October 13, 2008. Additionally, an affiliate of an insured depository institution may request that its federal banking regulator recommend to the FDIC that a determination be made that the affiliate is an eligible entity. The Program rule describes the factors the FDIC will consider in making its determination.

An entity will automatically be an eligible entity if it satisfied the definition on or before December 5, 2008. An entity that falls within the definition after December 5, 2008 may request permission from the FDIC to participate in the TLGP. If an eligible entity ceases to be, or to be affiliated with, a chartered and operating insured depository institution, it may no longer participate in the Program.

There are differences between the institutions able to participate in Treasury’s capital programs and the eligible institutions under TLGP. For example, Industrial Loan Companies that are FDIC insured would qualify for the FDIC Program, but would not be qualifying financial institutions covered by the Capital Purchase Program. In addition, Treasury will make the final determination of eligibility to qualify for a capital program in consultation with the institution’s primary banking regulator. The FDIC will coordinate with the primary regulator for supervisory purposes, but has not indicated that any special steps need to be taken to qualify for the Program. Each of the nine financial institutions that initially agreed to participate in the Treasury’s Capital Purchase Program also agreed to participate in the TLGP.

An eligible entity not interested in participating after the first 30 days was required to *affirmatively opt out* of the Program by December 5, 2008. Failure to opt-out of the Program resulted in an eligible entity becoming an eligible participant, subject to the fees and compliance requirements of the Program. Eligible entities could opt out of *either or both* of the programs (the DGP and the transaction account guarantee program). The opt-out is a *one-time* event and is a permanent decision for the duration of the TLGP.<sup>1</sup> All eligible entities within a holding company structure were required to make the same decision, together opting out of one or both programs under TLGP, or choosing to remain in the programs.

The FDIC maintains an opt-out list on its website at [www.fdic.gov/tlgp](http://www.fdic.gov/tlgp). The FDIC does not, however, post a list of the participating entities.

Although set up as an opt-out, entities participating in the DGP were required to file their intention with respect to participating in the long-term non-guaranteed debt program (described below) and to provide the FDIC with their issuance cap (described below).

### Definition of Senior Unsecured Debt

Debt covered by the Debt Guarantee Program includes senior unsecured debt issued on or after October 14, 2008 through June 30, 2009, subject to extension to October 31, 2009 as described below. The Program was initially

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<sup>1</sup> There is a limited exception for the merger of an entity that has opted out with an entity that is a participating entity. Upon filing of an application for merger of eligible entities, the entities may request a change in status under the TLGP, for example, a request that the resulting entity opt out of the program or be a participant in the program.

intended to capture newly-issued senior unsecured debt regardless of its maturity. However, the final rule excludes debt with a maturity of 30 days or less, if issued after the opt-out date.

The final rule provides a non-exclusive list of senior unsecured debt instruments that are covered by the guarantee for participating institutions as well as a non-exclusive list of excluded debt. The FDIC has stated that the Program “is not designed to encourage the development of or to promote innovative or complex sources of funding but to enhance the liquidity of the inter-bank lending market and senior unsecured bank debt funding.” The FDIC has interpreted very narrowly “innovative or complex” debt instruments.

Senior unsecured debt means unsecured borrowing, denominated in either U.S. dollars or a foreign currency, that:

- is evidenced by written agreement (including a trade confirmation),
- has a specified and fixed principal amount to be paid in full on demand or on a date certain,
- is non-contingent and contains no embedded options, forwards, swaps or other derivatives,
- is not by its terms subordinated to any other liability, and
- (after December 5, 2008) is issued with a stated maturity of more than 30 days.

The debt may pay interest at a fixed or floating rate, but the floating interest rate must be based on a single index of a Treasury bill rate, the prime rate or LIBOR.

Senior unsecured debt includes but is not limited to:

- federal funds purchased,
- promissory notes,
- commercial paper,
- unsubordinated unsecured notes, including zero-coupon bonds,
- U.S. dollar denominated certificates of deposit owed to an insured depository institution, an insured credit union as defined in the Federal Credit Union Act or a foreign bank<sup>2</sup>,
- U.S. dollar denominated deposits in an international banking facility of an insured depository institution owed to an insured depository institution or a foreign bank,
- U.S. dollar denominated deposits on the books and records of foreign branches of U.S. insured depository institutions that are owed to an insured depository institution or a foreign bank, and
- mandatory convertible debt.

The examples of exclusions from the definition of senior unsecured debt provided in the final rule are:

- any obligation with a stated maturity of one month,<sup>3</sup>
- obligations from guarantees or other contingent liabilities,
- derivatives,

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<sup>2</sup> The term “foreign bank” does not include a foreign central bank or other similar foreign government entity that performs central bank functions or a quasi-governmental international financial institution such as the IMF or the World Bank. References to debt owed to an insured depository institution, an insured credit union, or foreign bank mean owed to the institution solely in its own capacity and not as agent.

<sup>3</sup> This recognizes that certain instruments have stated maturities of “one month,” but have a term of up to 35 days because of weekends, holidays and calendar issues.

- derivative-linked products,
- debt that is paired or bundled with any other security,
- convertible debt,
- capital notes,
- the unsecured portion of otherwise secured debt,
- negotiable certificates of deposit,
- deposits in foreign currency and or other foreign deposits (unless expressly included as covered senior unsecured debt),
- revolving credit agreements,
- structured notes,
- instruments that are used for trade credit,
- retail debt securities,<sup>4</sup>
- any funds that regardless of form are swept from individual, partnership or corporate accounts held at insured depository institutions, and
- loans from affiliates, including parents and subsidiaries and institution affiliated parties.

Further, debt will not be guaranteed if the proceeds are used to prepay outstanding non-guaranteed debt. Under the final rule, the proceeds from the issuance of FDIC-guaranteed debt may be issued to prepay other FDIC-guaranteed debt, but may not be used to prepay outstanding non-guaranteed debt.

### Guaranteed Debt Issuance Cap

Under the TLGP, the FDIC will guarantee new senior unsecured debt in an amount up to 125% of the par value of senior unsecured debt outstanding as of September 30, 2008, that is scheduled to mature by June 30, 2009. (The extended DGP does not change the issuance cap calculation.) For purposes of determining the issuance cap, the eligible entity should include debt with maturities of 30 days or less, even though such debt will no longer be guaranteed if issued after the opt-out date. Senior unsecured mandatory convertible debt is excluded from the calculation. The issuance cap is calculated separately for each individual participating entity within a holding company structure. Each participating entity calculated its outstanding senior unsecured debt as of September 30, 2008, and provided that information – even if the amount of the senior unsecured debt was zero – to the FDIC on the election form.

If an eligible entity did not have any senior unsecured debt (other than federal funds) outstanding on September 30, 2009, its issuance cap is 2% of total outstanding liabilities. An affiliate of an insured depository institution that becomes an eligible entity upon application to a federal banking regulator and the FDIC, will have its issuance cap determined by the FDIC at the time it is designated an eligible entity.

On a case-by-case basis, the FDIC may grant a participating entity authority to temporarily exceed the 125% issuance cap, or reduce its issuance cap. Based on the supervisory information available to it, the FDIC also may restrict the authority of an entity to issue guaranteed debt to a level below the 125% issuance cap.

An insured depository institution may combine its issuance cap with that of a direct or indirect parent participant. Participants interested in combining issuance caps are required to make a written request to the FDIC and the

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<sup>4</sup> The FDIC's updated "Frequently Asked Questions" clarifies that retail debt securities are those debt instruments the marketing of which is targeted to retail investors, typically with small denominations. It does not include debt securities purchased in the secondary market by retail investors if the initial marketing was targeted to non-retail investors.

participant parent entity. Any use of a parent's capacity to issue guaranteed debt will reduce the amount available to the parent under its cap.

For participating entities, all newly-issued senior unsecured debt, up to the issuance cap, becomes guaranteed as and when issued. Generally, only after the participant has issued guaranteed debt up to the cap amount may it issue non-guaranteed debt. However, a participant may issue long-term non-guaranteed debt at any time if it has elected to participate in, and is paying the special fee for, the long-term non-guaranteed debt program described below.

### Issuance of Non-Guaranteed Debt

#### *Long-Term Non-Guaranteed Debt Program for Participating Entities*

Under the original Program, a participating entity could issue non-guaranteed debt only (1) after FDIC-guaranteed debt had been issued up to the issuance cap or (2) through participation in the long-term non-guaranteed debt program. By December 5, 2008, participating entities were required to notify the FDIC of their election to participate in the long-term non-guaranteed debt program. Upon making an election, the participant paid a nonrefundable fee. The long-term non-guaranteed debt program granted participating entities the ability to issue debt on a non-guaranteed basis, provided it matured after June 30, 2012.

#### *New Non-Guaranteed Debt Issuance Option*

As part of the extensions to the Program announced on March 17, 2009 (discussed below), all DGP participating entities are eligible to apply for a new non-guaranteed debt program.

Participating entities accepted into the new non-guaranteed debt program will be able to issue non-guaranteed debt of any maturity after June 30, 2009. The issuance is not conditioned on the participating entity having issued FDIC-guaranteed debt up to its issuance cap.

There will be no cost for participating in the new non-guaranteed debt program.

Although the FDIC received many comments at the time the TLGP was initially launched to permit unrestricted ability to issue non-guaranteed debt, it declined to do so. At the FDIC board meeting on March 17, 2009, staff and Board members noted the current goal of facilitating a transition from reliance on the FDIC guarantee to more normalized liquidity transactions. They discussed their earlier concerns regarding adverse selection undermining efforts to stabilize the banking and credit markets, specifically institutions obtaining the perceived benefit of Program participation without paying any assessment for the issuance of non-guaranteed debt. The adverse selection concerns have been superseded by efforts to transition from perceived reliance on FDIC-guaranteed debt.

### Extended DGP

On March 17, 2009 the FDIC announced the extension of the Program (extended DGP). Given the widespread use of the DGP and the limited amount of non-guaranteed debt issued by financial institutions, the FDIC seeks an orderly transition from the issuance of FDIC-guaranteed debt to traditional funding. Extension of the issuance date and maturity date, as well as expansion of the non-guaranteed debt issuance program, addresses this goal.

After publication of the interim rule in the Federal Register, the rule will be open for a brief 15 day comment period and will then be made final. We expect few, if any, changes from the interim rule described here.

The amendments do not alter the current issuance cap for participating entities. Under the Program, participating entities can issue an amount of guaranteed debt equal to 125% of their senior unsecured debt outstanding on September 30, 2008 that was scheduled to mature by June 30, 2009.

### ***Eligible Entities for Extended DGP***

Participating entities in the DGP may be eligible to utilize the extended issuance period and the extended guarantee period (“extended DGP”). The extended DGP is available to the following:

- All insured depository institutions (IDIs) that are DGP participating entities
- DGP participating entities, other than IDIs, that have issued FDIC-guaranteed debt prior to April 1, 2009
- DGP participating entities, other than IDIs, that haven’t issued FDIC-guaranteed debt before April 1, 2009, upon FDIC approval of an application

A non-IDI participating entity that has not issued FDIC-guaranteed debt before April 1, 2009 may, but is not required to, apply for approval to participate in the extended DGP.

The application to participate in the extended DGP will require disclosure to the FDIC of the same information currently required in other TLGP applications: summary of the applicant’s strategic operating plan, proposed use of debt proceeds, plans for retiring any FDIC-guaranteed debt, financial history, current condition and future prospects, potential risk to the FDIC and any other information requested by the FDIC. The FDIC indicates that approval may be conditional, including conditioned on a requirement to pledge collateral to the FDIC. The collateral would be held by the FDIC as security against the applicant’s obligation to repay the FDIC for any payments made under the guarantee. If the FDIC previously imposed limits or conditions on a participating entity, those remain in effect under the amendments.

Applications are due by June 30, 2009.

### ***Extension of Issuance Period***

The DGP permits new issuance of FDIC-guaranteed debt through June 30, 2009. Participating entities in the extended DGP can issue FDIC-guaranteed debt through October 31, 2009.

A non-IDI participating entity that either (1) doesn’t apply for extended DGP approval, or (2) has an application denied, may issue FDIC-guaranteed debt through June 30, 2009.

The FDIC notes that this extension aligns the termination of this Program with the final effective date of numerous Federal Reserve Board (Federal Reserve) programs. While the Federal Reserve has left open the option of further extending its programs, Federal Reserve programs are authorized under standing authority of Section 13(3) of the Federal Reserve Act, whereas the TLGP was authorized under a systemic risk exception to its statutory authority, requiring involvement of the Secretary of the Treasury, the President and the Federal Reserve. In approving the interim rule for the extended DGP, the FDIC concluded that the interim rule was necessary to further enhance the TLGP. Additional extensions may require reassessment of the October 13, 2008 systemic risk finding.

### ***Extension of Guarantee Period***

The DGP previously permitted issuance of FDIC-guaranteed debt, with the guarantee expiring on the earliest to occur of: maturity of the debt, mandatory conversion of the debt or June 30, 2012. For entities participating in the extended DGP, the guarantee on FDIC-guaranteed debt will expire on the earliest to occur of: maturity of the debt, mandatory conversion of the debt or December 31, 2012.

A non-IDI participating entity that either (1) doesn’t apply for extended DGP approval, or (2) has an application denied, may issue FDIC-guaranteed debt with the duration of the guarantee determined under the prior rule.

## **Mandatory Convertible Debt**

On February 27, 2009 the FDIC Board approved an interim rule to extend the TLGP to provide an FDIC guarantee for mandatory convertible debt. The FDIC, concerned with the ability of participating entities to roll maturing debt into new debt, expanded the Program to guarantee debt that mandatorily converts into common stock. The FDIC's goal is to provide "additional flexibility to obtain funding from investors with longer-term investment horizons." As we discuss below, there are a number of factors financial institutions should consider when evaluating this new Program.

### ***Mandatory Convertible Debt—Defined***

The definition of "senior unsecured debt" now includes "mandatory convertible debt." Mandatory convertible debt is defined as senior unsecured debt that is required by its terms to convert into common stock of the issuer on a fixed and specified date, which must be on or before the expiration of the guarantee. The debt can convert earlier if the issuer fails to make a timely payment under the instrument or upon merger or consolidation where the surviving institution is not the issuer.

### ***Issuance Cap Unchanged***

As noted above, participating entities are able to issue FDIC-guaranteed debt up to an issuance cap. The amendments to include mandatory convertible debt within the definition of senior unsecured debt do not increase the cap or change its calculation. Although mandatory convertible debt is now included within the definition of senior unsecured debt, the calculation of the issuance cap has been amended to specifically exclude any outstanding mandatory convertible debt in the calculation.

Given the success of the DGP, issuers may have issued FDIC-guaranteed debt up to their issuance cap, leaving them unable to utilize the new features of the Program. Even those issuers with available issuance capacity will need to consider carefully the benefits and limitations of the new Program.

### ***Approval Required***

FDIC approval is required to issue guaranteed mandatory convertible debt under the Program. Depending on the structure of the proposed mandatory convertible debt, additional bank regulatory applications and notices will be necessary<sup>5</sup> and the application to the FDIC must include a confirmation that the participating entity has made all applications and notices required under the Bank Holding Company Act, Home Owners' Loan Act, Change in Bank Control Act and with the primary federal banking regulator. Applications to issue guaranteed mandatory convertible debt must be received by the FDIC no later than June 30, 2009.

### ***Disclosure and Fees***

Provisions of the DGP rules requiring disclosure have been amended to include specific disclosure language for guaranteed mandatory convertible debt: The expiration date of the FDIC's guarantee is the earlier of the mandatory conversion date or the guarantee expiration, which for some issuers will be no later than June 30, 2012 and for others will be no later than December 31, 2012 (see "Extended DGP"). The assessment for the guarantee of mandatory convertible debt will be calculated based on the number of days until conversion, rather than maturity date.

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<sup>5</sup> For example, if conversion of the mandatory convertible debt into common stock will result in a holder owning 10% of a national bank's outstanding voting common stock, prior notice to the Office of the Comptroller of the Currency is required under the Change in Bank Control Act.

### ***Guaranteed Mandatory Convertible Debt Considerations***

Although the FDIC extended the TLGP to provide participating entities assistance in obtaining funding from investors with longer time horizons than June 30, 2012, the issuance of mandatory convertible debt may pose other issues for institutions. The FDIC-guaranteed mandatory convertible debt will not provide Tier 1 capital until conversion into common stock, significantly diminishing its appeal to financial institutions. Institutions will need to evaluate their anticipated capital needs and debt funding plans, as well as the accounting treatment for a convertible instrument. Issuers also may wish to consider related transactions that will minimize the dilutive effect associated with the issuance of mandatorily convertible instruments; however, the choices may be limited in light of other government program restrictions. For example, if an institution anticipates issuing a mandatory convertible debt security, and it is a participant in the Treasury's Capital Purchase Program or Capital Assistance Program, it may be subject to certain limitations on "repurchase" transactions, which, under ordinary circumstances might have been used to offset potential dilution. An institution also should consider whether, from a capital structure perspective, the issuance of a mandatory convertible debt security will be helpful. It is unlikely rating agencies will ascribe "equity credit" to a mandatory convertible debt security.

Market commentators, research analysts and rating agencies have been particularly focused on the "tangible common equity" position of our financial institutions. Traditionally, mandatory convertible instruments have been seen as boosting tangible common equity. The instrument currently available for issuance under the DPG, however, would have an adverse impact on tangible common equity.

Financial institutions consider carefully the executive compensation and corporate governance limitations under the various government programs as well as which program provides the best opportunity to transition from government investment to fully private ownership. Participation in the TLGP, unlike participation in the Treasury's capital programs, does not require compliance with the executive compensation requirements under the Emergency Economic Stabilization Act of 2008 and the related TARP programs. As a result, the Program may provide financial institutions the ability to issue government guaranteed, low-risk instruments to private investors, free from the restrictions imposed by participation in other government programs.

### **Payment of Claims**

#### ***Guarantee Coverage***

Under the Program, upon the uncured failure of the issuer of guaranteed debt to pay interest or principal, the FDIC will make the required payment. This payment guarantee provided in the final rule is a change from the interim rule that had provided for a payment only upon the receivership of an insured depository institution or bankruptcy of a holding company. If the FDIC is paying interest and principal on debt that remains outstanding after June 30, 2012 (or for debt with a guarantee expiring after December 31, 2012), it will have the right to elect to make a final payment of all outstanding principal and interest due through the date of final payment, without incurring a prepayment penalty.

Upon an uncured payment default, a demand for payment to the FDIC must be made by an authorized representative of all of the holders of the defaulted debt or an individual debtholder. For guaranteed debt issued on or after December 6, 2008, the participant is required under the terms of the master agreement to appoint a representative for such purposes. Individual holders of the debt will have the option to represent themselves. Demands must be made within 60 days of the default. Once guarantee payments commence, the representative and any individuals will be required to assign their debt to the FDIC to collect against the participant. The participant will be obligated to reimburse the FDIC for its guarantee payments, interest on any unreimbursed amounts at the non-default interest rate plus one percent and for all reasonable out-of-pocket expenses of the FDIC.

### ***Master Agreement***

Participating entities executed a master agreement no later than the opt-out date<sup>6</sup> and provided a copy to the FDIC no later than ten days thereafter. The master agreement is required to facilitate the payment guarantee by the FDIC and includes the following key terms:

- the participant is required to provide notice, within one business day, of any failure to pay interest on or principal of any indebtedness,
- governing documents of guaranteed debt must include the following required terms:
  - appointment of a representative that will make claims for payment under the guarantee, requiring the representative to give the FDIC notice within one business day of any payment default by the participant,
  - authorizing the assignment to the FDIC of the debt instrument when the FDIC commences making guarantee payments,
  - requiring surrender of the debt instrument to the FDIC if it elects to repay the debt in full while making guarantee payments, and
  - requiring FDIC consent to any amendment to the debt instrument that modifies principal, interest, payment, default or ranking,
- for guaranteed debt evidenced solely by a trade confirmation, the participant must use commercially reasonable efforts to have the holder of the debt execute a written agreement that includes the required terms,
- no document governing guaranteed debt may provide for automatic acceleration of debt upon a default by the participant while the FDIC guarantee is in effect or while guarantee payments are being made by the FDIC (default is not limited in this provision to payment defaults), and
- a representation by the participant that any document filed with or furnished to the Securities and Exchange Commission was materially accurate.

Participants are required to comply with the provisions of the master agreement in all issuances from and after December 6, 2008.

### **Fees, Assessments and Surcharges**

When announced on October 14, 2009, all eligible entities were automatically included in the Program. During the first 30 days no fees were assessed on eligible entities and no fees were assessed on eligible entities that opted out. Fees accrued from November 13, 2008 for participating entities.

The Program is funded through its fees, assessments and surcharges; it does not rely on taxpayer funding. All amounts collected (other than as described below under “New Surcharges”) are held in a segregated account and not included in the Deposit Insurance Fund (DIF). If, at the termination of the Program, there is a shortfall, it will be recouped through a special assessment on insured depository institutions. Any special assessment will be based on liabilities (rather than deposits), resulting in a greater burden on the largest institutions. If, at the termination of the Program, there are excess funds remaining, they are expected to be deposited in the DIF. All financial institutions whose deposits are insured by the FDIC will be subject to any special assessment, irrespective of their participation in the TLGP. Many community banks and banks not owned by holding companies expressed concern during the rulemaking comment process that, upon a shortfall, insured depository institutions would bear a disproportionate burden because holding companies would not be subject to the special

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<sup>6</sup> Entities becoming participating entities after December 5, 2009 would promptly deliver the master agreement to the FDIC after approval.

assessment. As a result of these comments, the FDIC created a surcharge for certain holding companies participating in the Debt Guarantee Program, as described below.

Beginning November 13, 2008, fees are assessed on (1) senior unsecured debt, other than overnight debt, issued from October 14 through December 5 and still outstanding on December 5, 2008 and (2) senior unsecured debt issued from December 6, 2008 through June 30, 2009 (or October 31, 2009, if applicable).

- Guaranteed debt with a maturity (or date of conversion in the case of mandatory convertible debt) of 180 days or less: 50 basis points per annum
- Guaranteed debt with a maturity (or conversion date) of 181-364 days: 75 basis points per annum
- Guaranteed debt with a maturity (or conversion date) of 365 days or greater: 100 basis points per annum
- A 10 basis point per annum surcharge will be assessed on a participating entity that is an affiliate of one or more insured depository institutions (generally holding companies), if those affiliated depository institutions represent less than 50% of the consolidated assets.
- The applicable fees will be doubled for all outstanding guaranteed debt if a participating entity issues debt represented as guaranteed in excess of its issuance cap. The FDIC may reduce the penalty fee upon a showing of good cause.

The fee will be assessed from the issuance date through the earliest of the maturity date, the conversion date or the expiration of the guarantee. Invoices will be generated through *FDICconnect* once a participating institution notifies the FDIC of its issuance of guaranteed debt.

### ***Long-Term Non-Guaranteed Debt Program***

If a participating entity is participating in the long-term non-guaranteed debt program under the Debt Guarantee Program, it pays a fee of 37.5 basis point times the issuance cap. The nonrefundable fee is collected by the FDIC in six equal monthly installments. As the participating entity issues guaranteed debt, the amounts invoiced for guaranteed debt will be offset by the fees paid for the long-term non-guaranteed debt program.

### ***New Surcharges***

New surcharges were announced in connection with the March 17, 2009 amendments to the Program. They apply to all DGP participants, and are as follows:

	Insured Depository Institutions	Non-Insured Depository Institutions
FDIC-guaranteed debt issued prior to April 1, 2009	No surcharge	No surcharge
FDIC-guaranteed debt issued from April 1, 2009 through June 30, 2009, and maturing on or before June 30, 2012:		
that matures, or mandatorily converts, less than one year from issuance	No surcharge	No surcharge
that matures, or mandatorily converts, one year or more from issuance	10 basis points	20 basis points
FDIC-guaranteed debt issued after June 30, 2009 and on or before October 31, 2009	25 basis points	50 basis points

	Insured Depository Institutions	Non-Insured Depository Institutions
FDIC-guaranteed debt issued on or after April 1, 2009 with a maturity date after June 30, 2012	25 basis points	50 basis points

Income from these surcharges will be deposited in the DIF. The FDIC has taken a series of actions as a result of concerns regarding the inequity of the TLGP fee system discussed above. In addition to the surcharge for certain holding companies, the FDIC has sought legislative changes to the emergency special assessment provisions of the Federal Deposit Insurance Act, seeking assessment authority over holding companies in the event an emergency special assessment is needed to cover the costs of the TLGP.

Additionally, the DIF is currently experiencing a low reserve rate. On February 27, 2009, the FDIC approved an interim rule to impose a special emergency assessment of 20 basis points on all IDIs. The banking industry responded with concerns that the proposed assessments would impede lending activity. In proposing the amendments to the DGP, the FDIC noted three goals. The first was to enhance equity between the participating institutions (those paying the surcharge) and the IDIs (those paying for any shortfall in the Program). The second is to replenish the DIF, and potentially reduce the amount of the proposed emergency special assessment announced on February 27, 2009. Finally, the surcharge is intended to wean participating institutions from the DGP by reducing the subsidy currently provided by the FDIC in the form of lower cost of funds.

#### Related Regulatory Action: SEC and OCC Securities and Exchange Commission Exemption

FDIC-guaranteed debt issued with a maturity no later than June 30, 2012, is exempt from the registration requirements of the Securities Act of 1933 (Securities Act). While the guidance from the SEC has not yet been updated to reflect the extension of the Program through December 31, 2012, we expect such guidance promptly. References in this section to June 30, 2012, should be read to mean the expiration of the guarantee under the Program. Recently, the Office of the Comptroller of the Currency (OCC) has confirmed that the exemption from Securities and Exchange Commission (SEC) registration based on the FDIC guarantee exempts FDIC-guaranteed debt from the registration requirements of Part 16 of the OCC's regulations.<sup>7</sup> As described in more detail below, national banks regulated by the OCC may wish to review their current debt programs to maximize their borrowing flexibility.

On November 24, 2008, in response to a request by the FDIC, the staff of the SEC issued a letter confirming that certain FDIC-guaranteed debt issued under the Debt Guarantee Program is exempt from registration under the Securities Act.<sup>8</sup> Under the FDIC's TLGP rule, FDIC-guaranteed debt issued under the Debt Guarantee Program is backed by the full faith and credit of the United States and the FDIC provides a guarantee of timely payment of interest and principal. The guarantee, however, only extends through June 30, 2012; debt issued with longer maturities loses the benefit of the guarantee after that date. The SEC letter confirms that FDIC-guaranteed debt maturing no later than June 30, 2012 is debt "guaranteed by an instrumentality of the United States." Section 3(a)(2) of the Securities Act exempts from the Securities Act registration requirements a security that is guaranteed by an instrumentality of the United States.

#### *Office of the Comptroller of the Currency Exemption*

Section 3(a)(2) contains a number of exemptions from SEC registration, including an exemption from registration for bank securities. Because banks are subject to the substantive regulation of banking regulators, they were

<sup>7</sup> OCC Interpretive Letter No. 1108 (January 26, 2009), available at <http://www.occ.treas.gov/interp/jan09/int1108.pdf>.

<sup>8</sup> Letter dated November 24, 2008 from the Office of Chief Counsel of the Division of Corporation Finance re: Debt Guarantee Program component of the Temporary Liquidity Guarantee Program of the Federal Deposit Insurance Corporation Incoming letter dated November 24, 2008 is available at <http://www.sec.gov/divisions/corpfin/cf-noaction/2008/fdic112408.htm>.

exempted from the registration requirements of the securities laws. The OCC, however, has an alternate registration requirement for the national banks it regulates, at 12 C.F.R. 16 (Part 16). Part 16.5 provides an exemption from the OCC registration requirements if a security is exempt from the SEC's registration requirement. To qualify for the Part 16.5 exemption from OCC registration, the exemption from SEC registration must be based on an SEC exemption "other than section 3(a)(2) (exemption for bank securities) and section 3(a)(11) (exemption for intrastate offerings)."

In its Interpretive Letter, the OCC confirmed that an SEC exemption based on part of Section 3(a)(2), other than the bank securities exemption, would exempt a security from the registration requirements of Part 16. The SEC exemption from registration available for FDIC-guaranteed debt is based on the Section 3(a)(2) exemption for securities guaranteed by an instrumentality of the United States, a provision other than the bank securities exemption. As a result, FDIC-guaranteed debt issued under the Debt Guarantee Program that matures no later than June 30, 2012, and is therefore considered guaranteed by an instrumentality of the United States, is also exempt from the registration requirements of the OCC.

National banks, in reliance on the Interpretive Letter, may issue FDIC-guaranteed debt, maturing no later than June 30, 2012, exempt from the registration requirements of both the SEC and the OCC.

### **Considerations**

In light of the extension of the Program, bank issuers and national banks may wish to consider enhancing current programs to issue SEC-exempt and, for national banks, OCC-exempt, debt, with more flexible terms than would be permitted absent the FDIC guarantee.

Additionally, potentially eligible entities that were not automatically covered by the TLGP and have considered applying to the FDIC for "participating entity" status may, given the extension of the Program, wish to reevaluate the benefits of seeking qualification to issue FDIC-guaranteed debt.

### **Notice Requirements**

*Notices to the FDIC.* Participants are required to notify the FDIC through *FDICconnect* of each issuance of guaranteed debt. The Chief Financial Officer (or equivalent officer) must certify to the FDIC that the issuance is within the issuance cap. Upon notification, the FDIC will generate a fee invoice for the related guaranteed debt.

*Notices to Counterparties.* Participants in the DGP are required to use the final rule's prescribed disclosure language in all written materials provided to lenders or creditors when issuing *either* guaranteed or non-guaranteed debt. A participant may be issuing non-guaranteed debt as part of the long-term non-guaranteed debt program, for issuances after the participant has reached its issuance cap or, after June 30, 2009 as part of the recently announced non-guaranteed debt issuance provisions. The disclosures are only required with respect to debt that is eligible for the guarantee; the participant does not have to provide disclosure when issuing ineligible debt.

Compliance with the notice provisions was required by December 19, 2008. Prior to that date, the final rule requires that participants provide adequate disclosures in a commercially reasonable manner. In addition, issuers of guaranteed and non-guaranteed debt instruments will need to assess the materiality of the FDIC guarantee, or its absence, in light of applicable securities law liabilities when evaluating what disclosures to make.

### **Authorization and Supervision**

The TLGP was established under the FDIC's authority to prevent a "systemic risk." The FDIC Improvement Act of 1991 authorizes the FDIC to take action when Treasury, upon a recommendation of the boards of the Federal Reserve and the FDIC and in consultation with the President, makes a determination of comparable systemic risk.

The final rule makes clear that the FDIC has the primary authority over the TLGP. While the FDIC will work with an eligible entity's primary federal regulator, the FDIC will make all final decisions regarding parameters, eligibility and continuing participation in the Program. Participation in the TLGP constitutes consent and acknowledgment by the eligible entity of the FDIC's authority, as well as permission to the FDIC to permit on-site reviews as needed to determine compliance with the Program.

As a result of the TLGP, banking regulators will be enhancing their supervisory framework to include a review of TLGP participation to assure appropriate use of the new guarantee and prevent rapid growth or excessive risk-taking. The FDIC will maintain control over eligibility for the Program, in consultation with each institution's primary federal regulator.

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#### Contacts

Amy Moorhus Baumgardner  
(202) 887-1532  
[abaumgardner@mofo.com](mailto:abaumgardner@mofo.com)

Oliver Ireland  
(202) 778-1614  
[oireland@mofo.com](mailto:oireland@mofo.com)

Anna Pinedo  
(212) 468-8179  
[apinedo@mofo.com](mailto:apinedo@mofo.com)

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