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Corporate & Financial Weekly Digest

Posted at 12:57 PM on January 21, 2011 by Jeffrey M. Werthan

FDIC Board Approves Interim Final Rule on New Liquidation Authority and Clarifies Treatment of Creditor Claims

The Board of Directors of the Federal Deposit Insurance Corporation (FDIC) voted on December 18 to approve an interim final rule clarifying how the agency will treat certain creditor claims under the new orderly liquidation authority established under the Dodd-Frank Wall Street Reform and Consumer Protection Act. Title II of the Dodd-Frank Act provides a mechanism for appointing the FDIC as receiver for a financial company if the failure of the company and its liquidation under the Bankruptcy Code or other insolvency procedures would pose a significant risk to the financial stability of the United States. FDIC Chairman Sheila Bair said: "The orderly liquidation process established under Title II of the Dodd-Frank Act imposes the losses on shareholders and creditors, while also protecting the economy and taxpayer interests. The interim final rule provides needed guidance to the market and underlines the clear statutory intent that creditors bear the losses of any failure. Shareholders and unsecured creditors should understand that they, not taxpayers, are at risk...."

The interim final rule approved today differs from the notice of proposed rulemaking by clarifying the standard for valuation for collateral on secured claims and by clarifying the treatment of contingent claims. In addition, the agency clarified that short-term debt holders are highly unlikely to meet the criteria set forth in the statute for permitting payment of additional amounts. In virtually all cases, holders of shorter-term debt will receive the same *pro rata* share of their claim that is being provided to the long-term debt holders. Accordingly, "a potential credit provider to a company subject to the Dodd-Frank resolution process should have no expectation of treatment that differs depending upon whether it lends for a period of over 360 days or for a shorter term."

The final rule follows a notice of proposed rulemaking and 30-day comment period. According to the FDIC, a majority of comments related to matters beyond the scope of the notice of proposed rulemaking, indicating the need for additional rulemaking in the future. The interim final rule also addresses discrete issues:

1. the authority to continue operations by paying for services provided by employees and others (by clarifying the payment for services rendered under personal services contracts);
2. the treatment of creditors (by clarifying the measure of damages for contingent claims); and

3. the application of proceeds from the liquidation of subsidiaries (by reiterating the current treatment under corporate and insolvency law that remaining shareholder value is paid to the shareholders of any subsidiary).

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