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FDIC Issues Final Rule under Orderly Liquidation Authority Provisions of Dodd-Frank Act

In a long awaited action, the Federal Deposit Insurance Corporation (FDIC) issued a final rule on July 6 which addresses the FDIC's rights and powers as receiver of a nonviable systemic financial company under the orderly liquidation authority provisions of Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Chairman Sheila Bair, conducting her last meeting before leaving the agency, stated that, "A fair amount of the goal of the orderly liquidation authority is to convince investors in large financial institutions that their money is at risk if the institution fails." The final rule will adopt with certain changes the proposed rule set forth in the Notice of Proposed Rulemaking (NPR) approved by the FDIC's Board on March 15 and also will incorporate, with certain changes, the Interim Final Rule (IFR) issued by the Board on January 18. Of particular interest is the so-called "claw-back" rule, which will allow the FDIC to recoup certain earnings of senior executives for mere negligence, as opposed to a higher standard of gross negligence. The final rule did not finalize the criteria for determining whether a company is predominantly engaged in activities that are financial in nature or incidental thereto, which will determine in part whether a company needs to write and submit for approval a "living will."

The final rule is divided into three subparts: A, B, and C. Subpart A, among other things, provides that (1) services rendered by employees to the FDIC as receiver for a covered financial company will be compensated according to the terms and conditions of any applicable personal service agreements, and that such payments will be treated as an administrative expense; (2) in the event that the FDIC acts as receiver for a direct or indirect subsidiary of an insurance company and that subsidiary is not an insured depository institution or an insurance company itself, the value realized from the liquidation of the subsidiary will be distributed according to the order of priorities set forth in the Dodd-Frank Act; (3) the FDIC will avoid taking a lien on some or all of the assets of a covered financial company that is an insurance company or a subsidiary that is an insurance company unless it determines that taking such a lien is necessary for the orderly liquidation of the covered financial company and will not unduly impede or delay the liquidation or rehabilitation of the insurance company or the recovery by its policyholders; (4) the FDIC as receiver of a covered financial company may recover from senior executives and directors who were substantially responsible for the failed condition of the company any compensation they received during the two-year period preceding the date on which the FDIC was appointed as receiver, or for an unlimited period in the case of fraud. Subpart A also clarifies the interpretation of provisions of the Dodd-Frank Act authorizing the FDIC as receiver of a covered financial company to avoid fraudulent or preferential transfers in a manner comparable to the relevant provisions of the Bankruptcy Code, so that transferees will have the same treatment in a liquidation under the Dodd-Frank Act as they would have in a bankruptcy proceeding.

Subpart B provides additional context and definition with respect to claims arising out of "amounts owed to the United States," and includes Section 380.24, which confirms the statutory treatment of claims arising out of the loss of setoff rights at a priority ahead of other general unsecured creditors if the loss of the setoff is due to the receiver's sale or transfer of an asset. Section 380.25 would finalize provisions addressing the determination of post-insolvency interest on unsecured claims. Section 380.26 clarifies the payment of obligations of bridge financial companies and the rights of receivership creditors to any remaining value upon termination of a bridge financial company. Subpart B also now includes at Section 380.27 the rule originally found at Section 380.2 of the IFR, clarifying that the FDIC would not use its discretion to differentiate among similarly situated creditors under Section 210 of the Dodd-Frank Act to give preferential treatment to certain long-term senior debt with a term longer than 360 days and that subordinated debt and equity never will qualify for preferential treatment.

Subpart C sets forth the administrative process for the determination of claims against a covered financial company by the receiver. This process will not apply to any liabilities or obligations assumed by a bridge financial company or other entity or to any extension of credit from a Federal reserve bank or the FDIC to a covered financial company. Similarly, the claims process will not modify any of the provisions of the Dodd-Frank Act regarding qualified financial contracts. Under the claims procedures, the receiver will publish and mail a notice advising creditors to file their claims by a bar date that is not less than 90 days after the date of the initial publication. Upon receipt, the receiver will have up to 180 days to determine whether to allow or disallow the claim, subject to any extension agreed to by the claimant. The claimant will have 60 days from the earlier of any disallowance of the claim or the end of the 180-day period (or any agreed extension) to file a lawsuit in federal court for a judicial determination. No court has jurisdiction over any claim, however, unless the claimant has complied with the requirements of the claims process. Subpart C also includes provisions concerning contingent claims and secured claims.

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