October 1, 2014

TO: Board of Directors

FROM: Bret D. Edwards Bret D Edwards
Director
Division of Resolutions and Receiverships

Richard J. Osterman, Jr. RJO
Acting General Counsel
Legal Division

SUBJECT: Proposed Rule to Revise 12 C.F.R. Part 340, "Restrictions on Sale of Assets by the Federal Deposit Insurance Corporation"

RECOMMENDATION

Staff recommends that the Board approve a notice of proposed rulemaking to revise 12 C.F.R. Part 340, "Restrictions on Sale of Assets by the Federal Deposit Insurance Corporation" ("Part 340"), in order to clarify the applicability of the rule, to make the rule more consistent with 12 C.F.R. section 380.13 ("Section 380.13"), which is the parallel provision in the FDIC's Orderly Liquidation Authority regulations that implements section 210(r) of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Section 210(r)" of the "Dodd-Frank Act"), 12 U.S.C. § 5390(r), and to make certain technical and conforming changes. The notice of proposed rulemaking, if approved by the Board, would request public comment on the anticipated revisions to Part 340.

DISCUSSION

Part 340 implements section 11(p) of the Federal Deposit Insurance Act, 12 U.S.C. 1821(p) ("Section 11(p)" of the "FDI Act"). Under Section 11(p), individuals or entities whose acts or omissions have, or may have, contributed to the failure of an insured depository institution cannot buy the assets of that failed insured depository institution from the FDIC. The FDIC expanded the purchaser eligibility restriction as permitted by statute when it promulgated Part 340 by precluding such individuals or entities from purchasing the assets of *any* failed insured depository institution, not only the particular institution affected by the actions of those individuals or entities. As provided in Section 11(p), Part 340 also prohibits the sale of assets involving FDIC financing to certain persons who have defaulted on obligations of $1 million or more, in aggregate, owed to a failed insured depository institution or the FDIC and who have made fraudulent misrepresentations in connection with any of those obligations. Compliance with Part 340 is established through a self-certification process by which a prospective purchaser certifies that it is eligible to purchase an asset from the FDIC and that the FDIC's sale of an asset to that prospective purchaser would not be restricted under Section 11(p) or Part 340.[1]

Section 210(r) of the Dodd-Frank Act is substantially similar to Section 11(p). Because Section 210(r) and Section 11(p) share substantially similar statutory language, Part 340 served as a model for the development of Section 380.13, which became effective on July 1, 2014. While many aspects of Part 340 were included in Section 380.13, FDIC staff identified new or different concepts to include in Section 380.13 that were not already in Part 340. Several of these concepts, if now incorporated into Part 340, would improve Part 340 and make it more consistent with Section 380.13. Staff is proposing to revise Part 340 as follows.[2]

The stated purpose of Part 340, set forth in paragraph 340.1(b), would be revised in order to prohibit sales of assets of a failed insured depository institution to individuals or entities who would also be prohibited from purchasing assets of a covered financial company under

[1] Staff intends to revise the existing Purchaser Eligibility Certification form after receiving comment from the public on the proposed revision to Part 340.

[2] A redline demonstrating staff's proposed changes to Part 340 can be found in Attachment C hereto.

Section 210(r) and Section 380.13. A corresponding change would be made in section 340.4 to include a prospective purchaser's ineligibility to purchase assets from the FDIC under Section 380.13 as a basis for ineligibility to purchase assets from the FDIC under Part 340. This change would ensure consistency among Part 340 and Section 380.13 as Section 380.13 precludes individuals or entities that are prohibited from purchasing assets of a failed insured depository institution from purchasing assets of a covered financial company.

Staff is proposing to change Part 340's scope of coverage in three ways to make it more consistent with Section 380.13. First, staff proposes to make clear that, consistent with existing practice, sales of assets by a subsidiary of a failed insured depository institution or by a bridge depository institution would fall within the scope of coverage if the FDIC controls the terms of the sale of assets of such subsidiary or bridge depository institution by agreement or as shareholder. Second, staff proposes a clarification that Part 340 does not apply to certain types of transactions involving marketable securities and other financial instruments that customarily are traded through a financial intermediary and where the FDIC, as seller, cannot control selection of the purchaser according to market convention. Third, staff proposes that language be included to clarify that Part 340 is not applicable to a judicial sale or a trustee's sale of property securing an obligation because, in such settings, the sale is not conducted or controlled by the FDIC.

Staff is proposing changes to definitions of terms used in part 340. The definition of "associated person" would be revised to include limited liability companies of which the prospective purchaser is a member if the prospective purchaser is an individual and, if the prospective purchaser is a limited liability company, to include the manager of the limited liability company. This updates the regulation, which was adopted before limited liability companies were in common use. The definition of "failed institution" would be revised to remove reference to entities "owned and controlled" by the failed institution because the revision to the scope of coverage, discussed above, explicitly states that sales of subsidiary assets are covered under Part 340 if the FDIC controls the terms of the sale by agreement or in its role as shareholder. Also, references to the Resolution Trust Corporation and RTC are removed in favor of generically referencing the FDIC's predecessor agencies. Additionally, staff is proposing to add a new term for use in part 340, "financial intermediary," to aid in identifying the types of transactions involving marketable securities and other financial instruments that Part 340 would not apply to, as discussed above.

Staff proposes to explicitly state in Part 340 that a prospective purchaser must certify that it is not using a straw purchaser or other subterfuge to allow it to purchase an asset from the FDIC or benefit from such transaction if such person would otherwise be ineligible to purchase assets from the FDIC under Part 340. The form certification presently in use[3] includes such a statement, but a comment submitted in response to the notice of proposed rulemaking to adopt Section 380.13 suggested that proposal be strengthened by including such language in the regulatory text itself. Staff recommends a corresponding change to Part 340.

From time to time, bridge depository institutions are used as a resolution method by the FDIC and they purchase assets of failed insured depository institutions. To address the question of whether a bridge depository institution must comply with the certification requirement, staff proposes that bridge depository institutions be included among the list of entities excepted from the self-certification requirement because it is reasonable to presume a bridge depository

[3] The Purchaser Eligibility Certification, FDIC Form 7300/06.

institution will be in compliance with Part 340 as such entity is subject to control or oversight by the FDIC.

Finally, staff is proposing to amend section 340.8, which provides that Part 340 does not apply if the sale resolves or settles a person's obligation to the FDIC, to also except a sale that resolves a claim that the FDIC has asserted against a person. This is not intended to be a substantive change but rather to more closely track Section 11(p), which excepts sales that resolve or settle either claims or obligations. This proposed change would ensure that the regulation cites both bases for exception set forth in the statute. It would also ensure consistency with the equivalent provision in paragraph (a)(2)(vi) of Section 380.13.

These proposed changes are intended to clarify the restrictions on sales of assets of failed insured depository institutions by the FDIC and will ensure consistency among Part 340 and Section 380.13, which will allow the FDIC to more efficiently administer the two rules and will help the public better understand the two rules.

CONCLUSION

It is recommended that the Board of Directors approve the revisions to Part 340 as proposed by staff and authorize publication of the attached Federal Register notice.[4]

Staff Contacts

Legal Division: Elizabeth Falloon, Supervisory Counsel, (703) 562–6148; Shane Kiernan, Counsel, (703) 562-2632.

[4] See Attachment A for model resolution and Attachment C for proposed Federal Register notice.

Division of Resolutions and Receiverships: Andrea Riche, (202) 898-7009; James D. Sigler, (202) 898-3871.

ATTACHMENTS

A – Resolution

B – Federal Register Notice

C – Part 340 Rule Text Blacklined to Show Changes

<u>Attachment B</u>

Notice of Proposed Rulemaking