FDIC Issues and Withdraws FAQs Regarding Its Private Equity Policy Statement

On December 11, 2009, the Federal Deposit Insurance Corporation (FDIC) issued frequently asked questions (FAQs) regarding its Final Statement of Policy on Qualifications for Failed Bank Acquisitions (PE Policy Statement). See FDIC Adopts Modified Guidelines for PE Investments in Failed Institutions: The Debate Continues, 21st Century Money, Banking & Commerce Alert® (Aug. 28, 2009). Almost immediately, the FAQs were withdrawn, for reasons that have not been made public. The withdrawn FAQs, which appear to be based on an ad hoc collection of questions, attempted to clarify several points. Numerous other questions that might have been addressed were not.

Partnerships or joint ventures between private equity investors (PE Investors) and an established bank or thrift holding company are exempt from the PE Policy Statement when the holding company holds a “strong majority interest.” The FAQs explain what constitutes a “strong majority interest.” A partnership or joint venture is generally exempt when the PE Investors hold no more than one-third of the total equity and the voting equity of the partnership or joint venture. Alternatively, if PE Investors invest directly in an established bank or thrift holding company, shareholders pre-dating that investment must retain at least two-thirds of the total equity of the holding company in order for the PE Investors to be exempt from the PE Policy Statement.

The withdrawn FAQs also spoke to the question of when PE Investors that hold 5% or less of the total voting power of an acquired bank, thrift or holding company are deemed to be engaged in concerted action with other investors, so as to aggregate their ownership interests and cause them to be considered to control 5% or more of the voting stock, which would bring them within the scope of the PE Policy Statement. While noting that the FDIC will generally defer to a determination made by the Federal Reserve Board or the Office of Thrift Supervision regarding investors acting in concert, the FAQs offered certain qualifications. First, if the FDIC is aware of “specific facts” that were not available to the primary federal banking agency, or there is present any one of several “special voting rights” that normally are indicative of control, the FDIC will make its own determination. Second, the use of a placement agent to solicit investors and the conduct by investors of a due diligence review of management will not, in and of themselves, constitute concerted action. The latter “clarification” may raise more questions than it answers as it seems to conflict with the long-held principle that a determination of concerted action focuses on the operation and management of a bank or holding company rather than the process of assembling investors and working through the investment or acquisition process.
Regarding how the FDIC would apply the 5% exclusion to convertible securities, the FAQs generally confirmed the customary approaches used by the federal banking agencies as to when such securities are considered to constitute the underlying common stock for purposes of control, and that, notwithstanding the form of investment, a resulting interest in 5% or more of the voting equity would trigger the application of the PE Policy Statement.

As we have noted in our past communications, the need to clarify the PE Policy Statement exists, in part, because its requirements exceed the various standards applied by the other federal banking agencies regarding control of a banking organization. This has raised questions regarding how conflicts or inconsistencies between those rules will be resolved. It is not clear whether the FDIC intends to collect a broader set of questions in a more formal or systematic manner, whether the other federal banking agencies have been or will be involved in the process, or when the FAQs might be re-released.

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