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Private Equity Investments in Financial Services Raising & Solving New Issues

The good news is that private equity ("PE") investments in financial institutions are occurring at an unprecedented pace, and there is a backlog of deals in active discussion with the FRB and the OTS. The better news is that with each new deal, the rules of the road are being clarified and the universe of potential structures is even being expanded as regulators and PE firms get comfortable with each other.

As these transactions are being considered, each one seems to have a slightly different structure and investor make-up, which in turn raises a variety of new issues for regulators and investors that the PE firms attempt to resolve through deal structures, terms and conditions that address the economic and business needs of the parties while still satisfying regulatory concerns. Most recently, the OTS approved the MaitlinPatterson Global Advisors LLC's application of ten (10) limited partnerships to acquire control of Flagstar Bancorp., Inc. (OTS Order 2009-06, Jan. 29, 2009), which reportedly facilitated the Treasury's approval of the bank's TARP assistance application.

Issues that are likely to be further clarified in the future include:

1. Acceptable structures and terms for PE consortiums purchasing failed banks from the FDIC (*e.g*, loss sharing, indemnification, shareholder/LLC agreements and financial terms).
2. The practical options provided by "shelf" and "inflatable" charters.
3. The role of PE firms in recapitalizing and qualifying banks that are applying for the CPP under TARP.
4. The impact of the CPP and the priority of the Treasury when CPP banks seek to recapitalize, merge or be acquired.
5. The range of provisions in shareholder and LLC agreements that are consistent with passivity commitments provided by investors.
6. The range of relationships between the investing parties that are consistent with commitments regarding not acting in concert.
7. The number and nature of director representation that investors may have under a variety of situations, and the independence of the bank's board of directors.
8. The role of capital commitments and source of strength agreements, particularly where the bank participates in the CPP.

9. Director interlock, cross guarantee, stock aggregation tracking and affiliate transaction issues.

10. How “silo” transactions will need to be structured from an economic and legal perspective.

We continue to be confident that the PE and regulatory worlds have enough good reasons to compromise fundamental principles in order to meet each other half way, and that in the current environment, transactions will continue to occur.

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