DAVIS POLK & WARDWELL

Temporary Liquidity Guarantee Program: FDIC Interim Rule

October 27, 2008

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The FDIC's Temporary Liquidity Guarantee Program (the TLG Program), which guarantees certain senior unsecured debt issued by eligible banking institutions and provides unlimited deposit insurance through 2009 for certain non-interest bearing transaction accounts, became effective on October 14, 2008, but it was not until the Interim Rule implementing the TLG Program was published on October 23, 2008 that the FDIC clarified specific features of the TLG Program. Eligible institutions have been covered by the TLG Program since October 14, 2008 free of charge, and will have to decide by November 12, 2008 whether to stay in or opt out of all or part of it. The FDIC has publicly stated its preference that most eligible institutions remain in the program, and the nine systemically important bank holding companies opted in early when accepting capital injections from Treasury, as has been widely reported. Rough estimates by the FDIC indicate that $1.4 trillion of debt would benefit from the debt guarantee and $400-$500 billion in deposits would benefit from the transaction account guarantee if all eligible institutions participate

The stated purpose of the TLG Program is to preserve confidence and encourage liquidity in the U.S. banking system and to ease lending to creditworthy businesses and consumers. Even after the publication of the Interim Rule, it is unclear how certain important features of the TLG Program – especially the timing and process for payments to lenders and investors under the FDIC's guarantee of senior unsecured debt issued by eligible holding companies – will be implemented. As a result, eligible institutions wishing to issue senior unsecured debt now or in the near future face the prospect of making decisions about the extent of their participation in the TLG Program, the consequences of their participation, and how to disclose the scope of the debt guarantee to the market, without having the full range of information that would normally be available.

The Interim Rule became immediately effective. It is, however, subject to a fifteen-day public comment period from publication in the Federal Register, which has not yet occurred. As a result of comments received, further changes may be made to the TLG Program although, as a practical matter, a final rule reflecting those changes is unlikely to be published until after the opt-out date, and it is unclear to what extent the FDIC will be able to respond to comments by the opt-out date. This memorandum is designed to help institutions identify the residual uncertainties of the TLG Program and the choices available to them.

Important Dates

» **Both Guarantees**

- **November 12, 2008**, 11:59 PM EST – opt out deadline
- **November 11-13** – estimated deadline for comments on Interim Rule (depending on publication in Federal Register)
- **December 1, 2008** – last date to notify FDIC of debt issued through and still outstanding on November 12, 2008 under guarantee
- **December 1, 2008** – effective date for disclosure requirements relating to participation in debt and transaction account guarantees ("adequate" disclosure "in a commercially reasonable manner" before then)

» **Debt Guarantee**

- **October 14, 2008** – first day for guarantee coverage of newly issued, senior unsecured debt
- **November 12, 2008** – last day for opt in to long-term non-guaranteed debt option
- **November 12, 2008** – last day to report senior debt outstanding at September 30, 2008 and scheduled to mature on or before June 30, 2009 (with CFO or equivalent's certification)
- **After November 12, 2008** – ongoing issuance notifications to FDIC (with "entity" certification)
- **June 30, 2009** – last day to issue debt under guarantee
- **June 30, 2012** – debt guarantee terminates (unless debt matured on earlier date)

» **Transaction Account Guarantee**

- **October 14, 2008** – unlimited coverage begins
- **December 31, 2009** – unlimited coverage ends

Overview of the Temporary Liquidity Guarantee Program

Core Features of the TLG Program

The TLG Program has two separate parts:

» A guarantee through June 30, 2012 or an earlier maturity date of certain senior unsecured debt issued by eligible institutions from October 14, 2008 through June 30, 2009 (the debt guarantee); and

» Unlimited deposit insurance through December 31, 2009 for certain non-interest bearing transaction accounts at FDIC-insured institutions (the transaction account guarantee).

The debt guarantee will not extend beyond June 30, 2012, regardless of whether guaranteed debt matures after that date, making the guarantee of little value for longer-term debt issuances. The Interim Rule acknowledges this by creating a limited opt-out, described in more detail below, for long-term debt. Institutions must pay significant up-front fees when selecting this option which are counted towards fees later incurred for issuing guaranteed debt.

Under the transaction account guarantee, the FDIC provides unlimited deposit insurance coverage for non-interest bearing transaction accounts at FDIC-insured institutions. This enhanced deposit insurance expires December 31, 2009, along with the temporary increase in general deposit insurance to $250,000 established by the Emergency Economic Stabilization Act of 2008.

All eligible institutions will be deemed to participate in both guarantee programs unless they opt out of one or both programs. The nine financial institutions designated as systemically important for purposes of the U.S. Treasury's capital purchase program – Bank of America, Bank of New York Mellon, Citigroup, Goldman Sachs, JPMorgan, Merrill Lynch, Morgan Stanley, State Street and Wells Fargo – have agreed to participate in both programs.

Starting November 13, 2008, after an initial period free of charge, fees will be assessed on institutions participating in the TLG Program as described in more detail below. If the fees collected are inadequate to cover the TLG Program's costs after any FDIC recoveries from failed institutions' estates, the difference will be covered by an assessment on all FDIC-insured depository institutions, not only those participating in the TLG Program, as provided for in the systemic risk exception of the Federal Deposit Insurance Act.

Eligible Entities

- FDIC–insured banks and thrifts
- U.S. bank holding companies with an FDIC-insured subsidiary
- Certain U.S. savings and loan holding companies (see text)
- Designated affiliates after consultation with their primary federal banking regulatory, only for the debt guarantee
- Insured branches of non-U.S. banks may participate only in the transaction account guarantee
- All branches of foreign banks are excluded from the debt guarantee

Eligible Entities

The following categories of institutions are eligible to participate in the TLG Program:

» FDIC-insured depository institutions, except that insured branches of non-U.S. banks may *not* participate in the debt guarantee;

» *Only* for participation in the debt guarantee, as holding companies themselves do not accept deposits and thus are not eligible to participate in the transaction account guarantee, U.S. bank holding companies (organized under the laws of any U.S. state or the District of Columbia), provided that they have at least one chartered and operating FDIC-insured depository institution within their holding company structure;

» *Only* for participation in the debt guarantee, as holding companies themselves do not accept deposits and thus are not eligible to participate in the transaction account guarantee, U.S. savings and loan holding companies (organized under the laws of any U.S. state or the District of Columbia), provided that they have at least one chartered and operating FDIC-insured depository institution within their holding company structure *and* either:

- engage only in the activities permissible for bank holding companies that have elected to become financial holding companies; or
- have, as of October 13, 2008, at least one FDIC-insured depository institution that had applied for authority to engage in certain non-banking activities under Section 4(c)(8) of the Bank Holding Company Act of 1956; and

» *Only* for participation in the debt guarantee, other affiliates of FDIC-insured depository institutions that the FDIC, in consultation with the relevant institution's primary federal banking regulator, designates as eligible entities. During the FDIC Board's open meeting on October

23, 2008 to approve the Interim Rule, the FDIC indicated that the factors it would consider in approving such an affiliate for eligibility would be the extent of the financial activities of the entities in the related holding company's structure, the ratings strength of the affiliate and the "size and extent of the activities of the organization."

Uninsured U.S. branches and agencies of non-U.S. banks are excluded from participation in both parts of the TLG Program.

Opt-out Period

All institutions eligible to participate in the TLG Program will be covered from October 14, 2008 through November 12, 2008 without charge. Before this 30-day period ends, institutions may opt out of one or both guarantee programs, at which point coverage ends. All entities in a bank or thrift holding company structure must make the same opt-out election for each part of the TLG Program, and are deemed to have opted out if their elections differ. Institutions which are not insured depository institutions need to make their election through their affiliated FDIC-insured depository institutions. The FDIC expects to make a form available for opting out in the week of October 27, 2008.

All entities in a bank holding company or thrift holding company structure must make the same opt-out election with respect to each part of the TLG Program, and are deemed to have opted out if their elections differ

If an institution fails to opt out or affirmatively opts in, participation becomes mandatory. The FDIC seeks broad participation in the TLG Program, and, as noted above, the nine most systemically important banking organizations have already agreed to participate. Many other eligible banking institutions may participate in at least the debt guarantee for fear of otherwise being excluded from the overnight funding market. Others may wish to avoid appearing on the list of institutions that opted out of either the debt or transaction account guarantees, to be published by the FDIC on its website, as required by the Interim Rule.

The Debt Guarantee

Senior Unsecured Debt

The Interim Rule provides greater clarity on the scope of "senior unsecured debt" than was previously available (see sidebar). To be eligible for the debt guarantee, debt must be evidenced by a written agreement, contain a specified and fixed principal amount to be paid on a date certain, and must be noncontingent and not subordinated by its terms to another liability.

The Interim Rule states that the primary purpose of the debt guarantee is to provide liquidity to the inter-bank lending market and promote stability in the unsecured bank funding market, not to encourage innovative, exotic or complex funding structures or to protect lenders who make high-risk loans in hopes of high returns. Eligible institutions considering the issuance of an instrument not listed among the included or excluded examples of senior unsecured debt should expect the FDIC to evaluate whether that instrument is eligible for the debt guarantee against this broad standard.

> The FDIC expressly excluded "exotic or complex" instruments such as derivatives, convertible notes and capital notes from "senior unsecured debt"

Maximum Guaranteed Amount

The maximum amount of FDIC-guaranteed debt that an institution may issue under the debt guarantee is 125% of the par or face value of the institution's senior unsecured debt outstanding as of September 30, 2008 that is scheduled to mature before June 30, 2009. The definition of "senior unsecured debt" used for eligibility purposes is also used to determine an institution's maximum guaranteed amount. This maximum guaranteed amount is calculated for each participating institution within the same holding company structure – *i.e.*, an insured depository institution, its affiliated bank or thrift holding company and any authorized affiliate each has its own cap – and each institution has an overall cap, not a cap for each debt type.

Senior Unsecured Debt

» **Included:**

- Federal funds purchased
- Promissory notes
- Commercial paper
- Unsubordinated unsecured notes
- Bank deposits in an international banking facility of an insured depository institution
- Certificates of deposit and Eurodollar deposits standing to the credit of a bank, *i.e.,* used for interbank funding
- Non-U.S. dollar-denominated senior unsecured debt

» **Excluded:**

- Obligations from guarantees or other contingent liabilities
- Derivatives, derivative-linked products
- Debt paired with any other security
- Convertible debt
- Capital notes
- Unsecured portion of otherwise secured debt
- Negotiable certificates of deposit
- Deposits in foreign currency and Eurodollar deposits that represent funds swept from individual, partnership or corporate accounts held at insured depository institutions
- Loans and other debt extended to affiliates or institution-affiliated parties

Fees Charged

- **75 bp for all covered debt (see text)**
- **150 bp on *all* guaranteed debt if the maximum guaranteed amount is exceeded**
- **Maximum guaranteed amount is 125% of senior unsecured debt outstanding as of September 30, 2008 scheduled to mature before June 30, 2009**
- **For those institutions that choose the long-term non-guaranteed debt option, 37.5 bp of 100% of all senior unsecured debt outstanding on September 30, 2008 with a maturity date on or before June 30, 2009**
- **Amounts issued under the Commercial Paper Funding Facility count towards the maximum guaranteed amount**
- **Fees are due when the debt is issued, except for long-term non-guaranteed debt option fee, which is paid in 6 equal installments and will be applied to offset other fees due the under debt guarantee**

The FDIC may allow, on a case-by-case basis, an otherwise eligible institution with zero qualifying debt outstanding as of September 30, 2008 to establish a maximum guaranteed amount in order to participate in the debt guarantee. Similarly, the FDIC may, in consultation with an institution's primary federal banking regulator, temporarily increase or decrease the institution's maximum guaranteed amount on a case-by-case basis.

> If an institution exceeds its maximum guaranteed amount, the fees on *all* of its outstanding FDIC-guaranteed debt doubles to an annualized 150 basis points

No debt issued by an institution in excess of its maximum guaranteed amount may be identified as FDIC-guaranteed. If an institution exceeds its maximum guaranteed amount and mistakenly or intentionally issues excess debt identified as guaranteed by the FDIC, the FDIC's assessments on all of its outstanding guaranteed debt doubles to 150 basis points and the institution and its affiliated parties would be subject to enforcement actions and assessments of civil money penalties. Although a penalty assessment *implies* that the excess debt will still be guaranteed by the FDIC, and although the FDIC has previously suggested that it will protect good-faith investors by extending the debt guarantee when the maximum guaranteed amount is exceeded, it would be preferable if the final rule explicitly clarified that good-faith investors and creditors would be able to rely on guarantee disclosure made available to them.

Participating institutions will need to put in place operational and compliance procedures to track outstanding guaranteed debt both for disclosure purposes and for keeping track of their maximum guaranteed amount. In this context, several aspects of the maximum guaranteed amount concept still need to be clarified. For example, it is unclear how an institution that is slightly below the maximum guaranteed amount could issue any meaningful amount of non-FDIC-guaranteed long term debt. The FDIC is expected to detail the procedures for calculating the maximum guaranteed amount shortly.

Institutions registered to sell commercial paper into the Federal Reserve's Commercial Paper Funding Facility (CPFF) should note that their issuance of commercial paper counts towards their maximum issuance amount under the debt guarantee, and that the FDIC will assess fees on such issuances, even

Changes/Clarifications to Debt Guarantee Provided by Interim Rule

- **"Senior unsecured debt" no longer includes unsecured portions of secured debt, excludes structured products, convertible notes and other products, and includes foreign currency denominated debt, certain CDs and Eurodollar deposits**
- **Exceeding maximum guarantee amount without clear disclosure that the excess is not guaranteed results in penalties**
- **Ability to issue non-guaranteed senior debt with maturity date after June 30, 2012 against up-front fee**
- **Guarantee pays in event of insolvency/receivership only, with risk of payment delays still to be addressed**

though institutions may think that participating in the CPFF obviates the need to use and pay for the FDIC guarantee. Institutions whose short-term debt rating will improve to at least A-1/P-1/F1 as a result of the FDIC guarantee might want to explore whether to also participate in the CPFF, which was not previously available to them. Institutions having access to the CPFF and who participate in the TLG Program will want to determine when to issue longer-dated debt in order to profit from the FDIC guarantee through June 30, 2012, given that the CPFF is currently scheduled to cease purchasing commercial paper on April 30, 2009 unless extended by the Fed.

Guarantee Fees

An annualized fee of 75 basis points multiplied by the amount of issued eligible debt will be imposed on all participating institutions for guaranteed debt issued (i) from October 14, 2008 through November 12, 2008, to the extent it remains outstanding after November 12, 2008, and (ii) from November 13, 2008 through June 30, 2009. The fee is assessed for the term of the debt, using June 30, 2012 as the maturity date for any debt maturing after June 30, 2012, and not assessing any fees for the period including November 12, 2008.

The FDIC's stated intent was to price the debt guarantee at a level slightly above normal market conditions, but "well below" current credit default spreads. Fees are due when debt is issued. No eligible debt is FDIC-guaranteed other than debt issued during the first free 30 days of the debt guarantee, until the fees for that debt are paid. Fees are not refundable for debt retired before its stated maturity.

Long-Term Non-Guaranteed Debt Option

Participation in the debt guarantee is "all or nothing" – all newly-issued senior unsecured debt will be guaranteed and an institution cannot issue non-FDIC-guaranteed debt until it has issued the maximum amount of guaranteed debt it is allowed at any point in time – except for the "long-term non-guaranteed debt option". If an institution elects this option, it enables the issuance of non-FDIC-guaranteed senior unsecured debt with a maturity date after June 30, 2012 at any time, in any amount, and without regard to the maximum guaranteed amount for that institution. Institutions must elect this option by November 12, 2008. Upon election, the institution must pay a non-refundable fee, collected in six equal installments, equal to 37.5 basis points of 100% of the institution's senior unsecured debt outstanding on September 30, 2008 with a maturity date on or before June 30, 2009. This non-refundable fee will be applied to offset the institution's debt issuance fees to the FDIC for guaranteed debt, if any, until the non-refundable fee is exhausted.

Participation in the debt guarantee is "all or nothing" except for the "long-term non-guaranteed debt option"

FDIC Payment of Claims Under the Debt Guarantee

The FDIC will pay out on guaranteed debt only when the issuing institution has entered receivership (in the case of FDIC-insured depository institutions) or bankruptcy (in the case of holding companies or other affiliates eligible for the debt guarantee, referred to in this memorandum as authorized affiliates) before the guarantee terminates on June 30, 2012. This is a somewhat limited guarantee compared to typical guarantees in commercial transactions, and it is more akin to insurance. The claims and payment processes differ significantly depending on which of these two cases applies, and there are significant unresolved issues and points of concern with respect to guarantee payments for the debt of bankrupt holding companies and their authorized affiliates. The FDIC appears to recognize this and seeks comments on how the claims process could be modified to speed payment without putting FDIC funds at risk.

Insured Depository Institution Debt

The FDIC's payments to holders of a failed insured depository institution's guaranteed debt will be made under the FDIC's existing receivership claims process set forth in Section 11 of the Federal Deposit Insurance Act. Under that process, the FDIC usually pays depositors of a failed insured depository institution by the next business day after entry into receivership. The FDIC has stated that it anticipates that "many debt holders, particularly sellers of federal funds", will be paid under its guarantee on the next business day after the failure of an insured depository institution. However, as the Interim Rule makes clear, under the usual procedure for determining claims other than those for insured deposits, holders of the guaranteed debt of an insured depository institution will have 90 days from the FDIC's publication of a notice to creditors to file their claims. The FDIC has 180 days after that filing to determine the amount guaranteed, and will pay interest at the 90-day Treasury Bill rate if payment takes longer than the next business day after receivership.

The guarantee's application to the debt of holding companies and their affiliates is complex, and FDIC payments may be significantly delayed

Bank Holding Company or Authorized Affiliate Debt

The process by which the FDIC will pay the holders of a bankrupt bank or savings and loan holding company's or its authorized affiliate's guaranteed debt is complex and time-consuming. This is in part because bankruptcy proceedings, especially Chapter 11 reorganizations for large institutions, are drawn-out and litigious affairs over which, unlike receivership of an insured depository institution, the FDIC has no direct control, although the Interim Rule does state that the FDIC will strive to "expedite the claims payment process". The conditions to FDIC payment in such a case are numerous.

First, the creditor's claim must be "allowed": the creditor must file a timely proof of claim in the bankruptcy proceeding and then file that proof of claim with the FDIC within 90 days of the proceeding's bar date. The process of establishing and filing such a claim can take up to one or two years, and even longer should the debtor or any creditor object to a claim.

Second, the FDIC does not have to pay a creditor unless and until the otherwise "allowed" claim is not subject to "reconsideration" under the Bankruptcy Code. The precise meaning of "reconsideration" is not spelled out in the Interim Rule and the FDIC's overall intent is not clear. One viable interpretation would allow the FDIC to prolong payment until the entire bankruptcy proceeding has been formally closed. During this ongoing process of establishing an "allowed" and "reconsideration-free" claim, the FDIC will pay interest, commencing on the filing of the bankruptcy petition, at the 90-day Treasury Bill rate in effect at the filing, which may not provide adequate protection to creditors as required under the Bankruptcy Code.

The Interim Rule does not expressly contemplate the fairly common situation in which creditors sell their bankruptcy claims in order to monetize their positions. Given the extended time it could take for debt holders to collect on the FDIC guarantee upon bankruptcy – a time frame incongruent with the relatively quick receivership payments the FDIC is known for – we believe the ability for holders of guaranteed debt to monetize their positions in an issuing institution's bankruptcy should be clearly stated in the final rule. Better, of course, would be an acceleration of the claims process, at least for holders of public company debt, which is unlikely to be disallowed.

We believe the ability for holders of guaranteed debt to monetize their positions in an issuing institution's bankruptcy should be clearly stated in the final rule

Restrictions on Use of Proceeds

The FDIC has declared that the debt guarantee should help to ensure that institutions are able to replace pre-existing, senior unsecured debt as it comes due. However, under the Interim Rule, proceeds from the issuance of guaranteed debt cannot be used to prepay existing debt before its stated maturity. As a result, institutions with broker-dealers that make a market in the institutions' own debt may not retire debt accumulated by the broker-dealer using the proceeds of its guaranteed issuances.

No Requirement to On-Lend

There is no express requirement that the funds raised from FDIC-guaranteed debt be used to grant loans, although the TLG Program was intended to enhance liquidity and the FDIC is encouraging eligible entities to use the capital raised to grant new loans.

Risk Weighting and Collateral

Institutions subject to regulatory capital requirements and that holding debt issued under the debt guarantee should benefit from favorable risk weighting. It is understood that the FDIC is encouraging 0% risk weighting for FDIC-guaranteed debt, but no final decision has been made yet by the Federal Reserve and other federal banking regulators.

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Finally, we expect that guaranteed debt will be accepted as collateral by the Federal Reserve Board.

Non-interest Bearing Transaction Accounts

- **Interest is neither accrued nor paid**
- **The institution does not reserve the right to require advance notice of an intended withdrawal**
- **Includes:**
  - Payroll accounts
  - Traditional demand deposit checking accounts
  - Official checks issued by an insured depository institution
  - Sweeps into non-interest bearing savings accounts
- **Excludes:**
  - Negotiable order of withdrawal (NOW) accounts
  - Money market deposit accounts

The Transaction Account Guarantee

Coverage

Under the transaction account guarantee, in addition to and separate from the existing deposit insurance limit, a temporary full guarantee is provided for funds held at FDIC-insured depository institutions in non-interest bearing transaction accounts. The intent of this guarantee is to cover payment-processing (*e.g.*, payroll) and other similar accounts. Funds in a non-interest bearing transaction account which are automatically swept into an interest-bearing account do not qualify for the transaction account guarantee, as the FDIC treats the funds as being in the account to which they were transferred. However, funds swept from a non-interest bearing transaction account to a non-interest bearing savings account are covered within the transaction account guarantee.

The FDIC seeks input on the effects of its decision to cover only non-interest bearing transaction accounts and exclude negotiable order of withdrawal (NOW) accounts, and seeks comments on whether excluding NOW accounts makes sense from a policy and deposit insurance standpoint.

Calculation of Fees

For the transaction account guarantee, an annualized assessment of 10 basis points will be paid on the balances in non-interest bearing transaction accounts that exceed the deposit insurance limit of $250,000, as determined on a quarterly basis by reference to the insured depository institution's call reports. Even in cases where a depositor maintains deposits in both an interest-bearing account and a noninterest-bearing account, the assessment would be on the balance in the noninterest-bearing account minus $250,000, *i.e.*, such amounts in the interest-bearing account would not be counted against the $250,000. Accounts with pass-through coverage will, according to the FDIC, be addressed considering each beneficiary's balance separately.

Payments in Receivership

The FDIC's payment obligations in connection with the transaction account guarantee follow established procedures. The FDIC is generally required to pay claims of depositors holding non-interest bearing accounts "as soon as possible" upon the failure of the institution. In most cases, the FDIC expects

Required Disclosure and Reporting

» **Institutions must report debt amount forming basis for calculating maximum guaranteed amount by November 12, 2008 even if it is zero**

» **Institutions must report, with CFO or equivalent certification, balances outstanding, debt issuances and instances of exceeding debt limit to FDIC**

» **For each debt issuance, institution must identify whether debt being offered is guaranteed, and if guaranteed, must be clearly identified as "guaranteed by the FDIC"**

» **For each guaranteed debt issuance:**

- Institution must notify FDIC of issuance;
- Institution and its CFO or equivalent must certify that issuance does not exceed guaranteed amount limit

» **Disclosure required for FDIC-insured institutions regarding transaction account guarantee**

payment to be made within one business day following a participating institution's failure, by making a new insured deposit of like amount available at another insured depository institution. If the account cannot be transferred to another insured depository institution, the FDIC will mail a check for the full amount of the guaranteed deposit "within days". Although the FDIC retains the discretion to require a depositor to file a proof of claim, the FDIC has stated that it does not anticipate that a proof of claim will ordinarily be required.

Disclosure and Reporting Required by the Interim Rule

In addition to the FDIC's publication of the lists of those institutions which opt out of the TLG Program, institutions participating in the debt or transaction account guarantees will be required to make disclosures to the FDIC and to potential lenders or customers.

Reporting to the FDIC

Any institution not opting out of the debt guarantee must notify the FDIC of any guaranteed debt it issued from October 14, 2008 through, and still outstanding, on November 12, 2008 even if it is zero by December 1, 2008, and must notify the FDIC of any guaranteed debt issued after November 12, 2008 within a specified time from issuance to be determined by the FDIC. Each institution must further report the amount of its senior debt forming the basis for its maximum guaranteed amount no later than November 12, 2008, and must regularly report debt issuances, balances outstanding and instances of exceeding its issuance limit, and each such report must contain a certification by the institution's CFO or equivalent. These notifications are to be made through the FDIC's existing e-business website, FDIC*connect*. For any issuance of guaranteed debt, the institution and its CFO or equivalent must provide the FDIC with a certification that the debt issued does not exceed the institution's guaranteed amount limit. The FDIC will publish procedures for these notice and disclosure requirements.

Disclosure to Potential Lenders and Investors at Each Debt Issuance

Effective December 1, 2008, each institution participating in the debt guarantee must clearly identify, in writing and in a commercially reasonable manner, to any interested lender or investor whether or not the debt it is offering is FDIC-guaranteed. Before December 1, "adequate" disclosure should be made in a "commercially reasonable" manner. To the extent clarity is achieved in the final rule that good-faith investors and creditors will be able to rely on the guarantee disclosure and be protected by a deemed guarantee, the diligence process involved has to be worked out, *e.g.*, whether institutions will have to provide representations as to their debt outstanding and the calculation of their issuance limit.

Disclosure Under the Transaction Account Guarantee

Every FDIC-insured depository institution must provide, in the lobby of its branches and main office, a notice of whether it is participating in the transaction account guarantee, and if participating, must also disclose that funds held in non-interest bearing transaction accounts are fully FDIC-insured. If the institution uses sweep arrangements or takes other actions that result in funds being transferred or reclassified to an interest-bearing account or nontransaction account, the institution must disclose those actions to affected customers and clearly advise them, in writing, that such actions will void the FDIC's guarantee.

FDIC Oversight

All institutions that participate in the TLG Program will be subject to oversight by the FDIC for compliance with the terms of the TLG Program. By participating, they agree to be subject to the FDIC's authority to request information and conduct on-site reviews to determine such compliance. When the TLG Program was first announced, the FDIC's oversight was described as aimed at preventing rapid growth or excessive risk-taking. Participation in the TLG Program does not result in a change in any participating institution's primary federal banking regulator.

All institutions that participate in the TLG Program will be subject to oversight by the FDIC for compliance with its terms

An institution's primary federal banking regulator, if not the FDIC itself, will, according to the Interim Rule, consult with the FDIC in enforcing the provisions of the Interim Rule.

Practice Pointers for Debt Issuances

Institutions may wish to issue guaranteed debt in the form of credit facilities or capital markets issuances on a registered or unregistered (Rule 144A) basis. In all cases, we expect that lenders and underwriters will:

- In the case of debt issued before November 12, 2008, include a covenant that the institution has opted in, or will not opt out, of the program;
- Undertake appropriate due diligence as to the institution's previous issuance history to ensure that the debt will be guaranteed and not exceed the limits;

Guaranteed debt may be issued from an institution's shelf registration statement

- Include a covenant to ensure that FDIC fees are paid when due, and may even consider imposing a condition precedent to closing that the fees be paid prior to closing; and
- Ensure that appropriate and prominent disclosure of the FDIC guarantee is provided.

Additional determinations will be required in the case of capital markets offerings, particularly in light of the fact that the FDIC's guarantee is considered a "security" that is being offered in connection with the capital markets transaction.

- Because the FDIC is an agency of the United States, the guarantee is exempt from registration under the Securities Act of 1933 and therefore institutions can continue to use their existing shelf registration statements without the need to amend them to add the FDIC's guarantee as a new security;
- While the guarantee is exempt from registration, institutions and underwriters will need to ensure that appropriate disclosure is included describing the FDIC's guarantee and its precise terms and limits, including that the guarantee is only a guarantee of payment in insolvency, and, particularly for entities other than insured depository

institutions, the potential for delays in collection during bankruptcy and the different calculation for post-petition interest;

- We do not expect that institutions will include any significant disclosure about the FDIC in their offering documents, given that the FDIC is an agency of the United States;
- Underwriters will likely seek counsel to provide "10b-5 statements" that will cover the offering document, including the description of the guarantee; and
- Underwriters will need to consider the appropriate level of due diligence necessary about the issuing institution in light of the existence of the guarantee.

Next Steps – Request for Comments

The FDIC invites comments on all aspects of the TLG Program as described in the Interim Rule, and seeks suggestions for its implementation. In particular, it seeks input on:

- » Ways to expedite the claims process in bankruptcy or receivership for the debt guarantee without putting FDIC-guaranteed funds at risk;
- » Whether to include NOW accounts in the transaction account guarantee; and
- » How to establish more effective means to achieve the purpose of the Interim Rule's disclosure provisions.

The FDIC is also expected to issue detailed procedures regarding the calculation of the maximum guaranteed amount per participating institution, the procedures for providing the notice and certification required in connection with each issuance of guaranteed debt and procedures for opting out of the TLG Program.

Below are hyperlinks to selected FDIC releases issued on Thursday, October 23, 2008:

- » Interim Rule
- » Chairman's Speech on the TLG Program
- » FDIC Press Release

We will continue to monitor developments and issue additional newsflashes and memoranda as we consider necessary.

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