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Down from the Shelf: Special Charter Used to Purchase Failed Bank

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Private equity investors long intrigued with the idea of investing in failed depository institutions can now point to a novel success story. On January 22, the Office of the Comptroller of the Currency (OCC) approved the initial use of a "shelf charter" to facilitate the purchase of Premier American Bank, a state-chartered bank closed that same day by the Florida Department of Financial Services.

The OCC had granted this group of investors preliminary approval to obtain a national bank charter, in October 2009. This status enabled the investors to enter a pool of potential bidders assembled by the Federal Deposit Insurance Corporation (FDIC) prior to the receivership of the failing bank.

In order for an acquirer to engage in an FDIC transaction (which are frequently assisted transactions) involving the assumption of deposit liabilities of a failed bank or thrift, the acquirer must have a bank or thrift charter. The process of acquiring such a charter is normally a time-consuming, months-long exercise not conducive to an investor who will receive scant notice of an opportunity to bid on a failing bank. The shelf charter, or OCC preclearance, enables an investor or investing group to resolve its regulatory issues in advance and to obtain a seat at the bidding table. The bank regulators will nonetheless conduct a rigorous review of the shelf bank's proposed management team, capital resources, and modified business plan, and final charter approval will not occur until the shelf bank's bid to acquire the failed institution is accepted by the FDIC. At that time, the chartering regulator will also demand a comprehensive business plan focused on the assets and liabilities actually being acquired. The entity must also obtain FDIC approval for deposit insurance, and depending upon the structure of the investor(s), obtain Federal Reserve approval to become a bank holding company or Office of Thrift Supervision approval to become a thrift holding company.

Potential new bank investors have been understandably confused by the bank regulators, whose interest in enticing new capital into an industry that desperately needs it appears to them to wax and wane. A series of regulatory actions in 2008—the issuance of an "inflatable" charter to J. Christopher Flowers in August 2008, the conditional preliminary approval for a shelf charter to the Ford Group Bank N.A. in November 2008, a new policy statement on Equity Investments in Banks and Bank Holding Companies issued by the Federal Reserve in September 2008, and the issuance of a modified bidder qualification process by the FDIC in November 2008—seemed to signal a new regulatory flexibility, aimed at getting private equity money and investors off of the sidelines and into the bidding game for failing banks and thrifts. The Office of Thrift Supervision also contributed a "preclearance" program in order to grant advance preliminary approval to new investors so that they might bid on troubled banks and thrifts.

But some cold water was thrown on investor hopes by the FDIC's Proposed Statement of Policy on Qualifications for Failed Bank Acquisitions published for comment in July 2009. The proposal requested comment on the FDIC's preliminary views as to investor capital commitments, source of strength expectations, limits on transactions with affiliates, concern as to secrecy law jurisdictions, and continuity of ownership requirements. Many commentators on the proposal voiced concern that its limitations and restrictions would deter many private capital investors from competing for the assets and liabilities of failed banks. The FDIC modified some of its positions in the Final Statement of Policy on Qualifications for Failed Bank Acquisitions issued on August 26, 2009, and noting that private capital funds joining together to purchase failed banks and thrifts was a recent phenomenon, and that it had already seen multiple variations in structures, promised to review its posture within six months.

Anyone viewing the FDIC's upward revisions as to the number of troubled banks, its proposed budget for 2010, or the opening of yet another FDIC "Temporary Satellite Office" can once again confirm the truism that bank failures are late casualties in a time of general economic distress. The unfortunate demise of hundreds of additional banks and thrifts will undoubtedly test the creativity of bank regulators and the daring of private equity investors. Thanks to the Premier American Bank transaction, there is now a better roadmap for investors to follow.

If you have any questions or would like more information on any of the issues discussed in this LawFlash, please contact author Kathleen W. Collins, or Jedd H. Wider, partners in Morgan Lewis's Business and Finance Practice:

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