BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

DIVISION OF BANKING
SUPERVISION AND REGULATION

SR 94-30 (FIS)

April 29, 1994

**TO THE OFFICER IN CHARGE OF SUPERVISION
AT EACH FEDERAL RESERVE BANK**

SUBJECT: **Written Agreements with Holding Companies of Banks Subject to Prompt Corrective Action**

Section 131 of the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") added section 38 of the Federal Deposit Insurance Act (the "FDI Act") (12 U.S.C. 1831o) ("Section 38"). Section 38 and the regulations issued thereunder by the Board of Governors, contained in the Board's Regulation H (12 C.F.R. Part 208, Subpart B), prescribe certain mandatory, and permit certain discretionary, corrective actions to be taken against undercapitalized[1] state member banks. The mandatory actions include a requirement that the bank file a capital restoration plan within 45 days of the date that the bank has received or is deemed to have received notice that it is in an undercapitalized condition.

Under Section 38(e)(2)(C) of the FDI Act, a state member bank's capital restoration plan may not be approved by the Board of Governors unless each holding company of the bank has guaranteed that the bank will comply with the plan until the bank has been adequately capitalized on average during each of four consecutive calendar quarters. Under this statute, the holding company also must provide appropriate assurances of its performance under the guarantee.[2] Two issues are raised by these statutory requirements: (1) the form of guarantee necessary in order to provide the Board of Governors with the ability to enforce it against the holding company, should the need arise; and (2) the content of the guarantee. Discussed below is Board staff's view of the appropriate form and content of guarantees for the parent holding companies of state member banks. Also discussed is the approach that generally should be taken vis-a-vis the holding companies of undercapitalized banks for which the Board of Governors is not the primary federal regulator.

Holding Companies of State Member Banks

With respect to state member banks, the staffs of the Board's Legal Division and this Division have determined that a resolution of the holding company board of directors detailing the steps to be taken under the subsidiary bank's capital restoration plan and a formal action, generally in the form of a Written Agreement between the appropriate Federal Reserve Bank and the holding company,

will be the acceptable form of guarantee.

The formal action should, at a minimum, contain two major substantive provisions:

(1) A limitation on the payment of dividends by the holding company without the prior approval of the Federal Reserve Bank and the Director of the Division of Banking Supervision and Regulation; and

(2) an agreement by the holding company that it will take all actions required of it under the bank's capital restoration plan, as specified in a resolution of the holding company's board of directors to be adopted concurrently with the signing of the formal action.[3]

Included in the second provision is the agreement of the holding company to undertake to cause the subsidiary bank to take all actions necessary to comply with its capital restoration plan and to a provision that would protect the subsidiary bank (or the Federal Deposit Insurance Corporation (the "FDIC"), as the case may be), in the event of the bankruptcy of the holding company.

The standard form of the resolution to be adopted by the board of directors of the holding company of a state member bank is Attachment A. A model Written Agreement with such a holding company (that solely addresses the guarantee issues) is Attachment B.

When requesting Board staff approval of a formal action containing a holding company guarantee, the Federal Reserve Bank staff should submit for review both the proposed formal action and the proposed resolution to be adopted by the holding company's board at the same time that it submits the recommendation for acceptance of the state member bank's proposed capital restoration plan.

Holding Companies of Non-State Member Banks

In the case of holding companies of national and state nonmember banks, the appropriate form of holding company guarantee is an issue committed to the discretion of the bank's primary federal regulator.[4] However, in certain cases, it may be appropriate to strengthen the enforceability of the holding company guarantee through a Written Agreement or other enforcement action between the Board and the holding company. In some cases, the primary federal bank regulator of national and state nonmember banks may request our assistance in strengthening the enforceability of the holding company guarantee through an enforcement action. For larger companies where the bank holding company's name is synonymous with the public's recognition of the bank (even when the holding company essentially is a shell), or where the bank holding company has assets which could be used to support the guarantee, consideration should be given to pursuing formal actions in a manner consistent with existing enforcement guidelines.

In all situations in which the Federal Reserve Banks otherwise would recommend a formal action against a bank holding company that has a state nonmember or national bank subsidiary and the subsidiary bank is operating under a prompt corrective action capital restoration plan approved by its primary federal regulator, our formal action should include the additional "WHEREAS" clauses

and the substantive provision set forth in Attachment C, in lieu of our standard capital provision.

If you have any questions regarding this letter, please contact Ann Marie Kohlligian, Senior Counsel, at (202) 452-3528, or Mary Frances Monroe, Senior Attorney, at (202) 452-5231.

signed by
Stephen C. Schemering
Deputy Director

Attachments:

Attachment A (PDF)

Attachment B (PDF)

Attachment C (PDF)

Notes:

1. As used in this context, the term "undercapitalized" also encompasses banks that are significantly or critically undercapitalized within the meaning of Regulation H.
2. A foreign bank that directly owns a U.S. bank (without an intervening U.S. holding company) likewise is a holding company subject to section 38(e)(2)(C) of the FDI Act.
3. In those cases in which a Federal Reserve Bank otherwise would recommend the imposition of a formal enforcement action against a bank holding company for reasons apart from the need for a guarantee of the subsidiary bank's plan (e.g., operating deficiencies, law violations, etc.), the two provisions detailed above should be included, along with such additional provisions as are necessary to address other problems.
4. The FDIC has directed its regional offices to provide to the appropriate Federal Reserve Bank copies of all proposed capital restoration plans, including the holding company guarantees, submitted by state nonmember bank subsidiaries of bank holding companies, in order to solicit the views of the Federal Reserve Banks with respect to whether the holding company's assurances of performance under the guarantee are realistic and not unduly risky. The Office of the Comptroller of the Currency has yet to provide guidance to their district offices regarding this matter.