

# Proposed Rules

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This section of the FEDERAL REGISTER contains notices to the public of the proposed issuance of rules and regulations. The purpose of these notices is to give interested persons an opportunity to participate in the rule making prior to the adoption of the final rules.

## FEDERAL DEPOSIT INSURANCE CORPORATION

### 12 CFR Part 360

RIN 3064-AC28

#### Treatment by the Federal Deposit Insurance Corporation as Conservator or Receiver of Financial Assets Transferred by an Insured Depository Institution in Connection With a Securitization or Participation

**AGENCY:** Federal Deposit Insurance Corporation.

**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** The Federal Deposit Insurance Corporation (the FDIC) is publishing for notice and comment a proposed rule regarding the treatment by the FDIC, as receiver or conservator, of financial assets transferred by an insured depository institution in connection with a securitization or in the form of a participation. The purpose of the rule is to resolve issues raised by Statement of Financial Accounting Standards No. 125 (SFAS 125), as promulgated by the Financial Accounting Standards Board (FASB), as to whether the FDIC's statutory authority to repudiate contracts pursuant to section 11(e) of the Federal Deposit Insurance Act (12 U.S.C. 1821(e)) would prevent a transfer of financial assets by an insured depository institution in connection with a securitization or in the form of a participation from satisfying the "legal isolation" condition of SFAS 125. Failure to satisfy this condition would prevent such a transfer from being accounted for as a sale in financial statements and reports prepared in accordance with generally accepted accounting principles (GAAP).

The proposed rule provides that the FDIC shall not, by exercise of its statutory power to repudiate contracts, recover, reclaim, or recharacterize as property of the institution or the receivership financial assets that were transferred by an insured depository institution in connection with a

securitization or in the form of a participation, provided that the transfer meets all conditions for sale accounting treatment under GAAP, other than the "legal isolation" condition as it applies to an institution for which the FDIC may be appointed as conservator or receiver, which the proposed rule is intended to address. The proposed rule defines both "securitization" and "participation," with "participation" specifically limited to participations that are "without recourse" to the selling or "lead" institution. The proposed rule does not apply unless the insured depository institution received adequate consideration for the transfer of financial assets at the time of the transfer, and the documentation effecting the transfer of financial assets reflects the intent of the parties to treat the transaction as a sale, and not as a secured borrowing, for accounting purposes. The proposed rule shall not be construed as waiving or limiting any other rights or powers of the FDIC as conservator or receiver of an insured depository institution to take any action or exercise any power not specifically addressed in the rule, including but not limited to any rights or powers of the FDIC regarding any transfer taken in contemplation of the institution's insolvency or with the intent to hinder, delay, or defraud the institution or the creditors of such institution. The proposed rule also provides that the FDIC shall not seek to avoid an otherwise legally enforceable securitization agreement or participation agreement executed by an insured depository institution solely because such agreement does not meet the "contemporaneous" requirement of sections 11(d)(9), 11(n)(4)(I), and 13(e) of the Federal Deposit Insurance Act.

The proposed rule may be repealed by the FDIC upon 30 days notice and opportunity for comment provided in the **Federal Register**, but in the event of such repeal, the rule shall continue to be effective with respect to any transfers made before the date of the repeal.

**DATES:** Written comments must be received by the FDIC on or before November 8, 1999.

**ADDRESSES:** Send written comments to Robert E. Feldman, Executive Secretary, Attention: Comments/OES, Federal Deposit Insurance Corporation, 550 17th Street, N.W., Washington, D.C. 20429. Comments may be hand delivered to the

guard station located at the rear of the 17th Street building on F Street on business days between 7:00 a.m. and 5:00 p.m. [FAX number (202) 898-3838, Internet address: [comments@FDIC.gov](mailto:comments@FDIC.gov)]. Comments may also be inspected and photocopied at the FDIC Public Information Center, room 100, 801 17th Street, N.W., Washington, D.C. between 9:00 a.m. and 4:30 p.m. on business days.

#### FOR FURTHER INFORMATION CONTACT:

Michael Krimminger, Division of Resolutions and Receiverships, (202) 898-8950; Robert Storch, Division of Supervision, (202) 898-8906; or Thomas Bolt, Legal Division, (202) 736-0168, Federal Deposit Insurance Corporation, 550 17th Street, N.W., Washington, D.C. 20429.

#### SUPPLEMENTARY INFORMATION:

##### I. Background

Under generally accepted accounting principles, a transfer of financial assets is accounted for as a sale if the transferor surrenders control over the assets. One of the conditions for determining whether the transferor has surrendered control is that the assets have been isolated from the transferor, i.e., put presumptively beyond the reach of the transferor, its creditors, and a trustee in bankruptcy or a receiver. This is known as the "legal isolation" condition. Where the transferor is an insured depository institution for which the FDIC may be appointed as conservator or receiver, the issue arises whether financial assets transferred by such institution in connection with a securitization or in the form of a participation would be put beyond the reach of the FDIC as conservator or receiver for such institution in light of (i) the statutory authority of the FDIC to repudiate contracts to which such institution is a party and (ii) the provisions of sections 11(d)(9), 11(n)(4)(I), and 13(e) of the Federal Deposit Insurance Act regarding the enforceability of agreements against the FDIC. The specific issues are whether the FDIC might, in the exercise of its authority to repudiate contracts, avoid a transfer of financial assets in connection with a securitization or in the form of a participation, and recover such assets; and whether the FDIC might, with respect to an agreement executed in relation to a transfer of financial assets in connection with a securitization or

with respect to a participation, assert the requirement of sections 11(d)(9), 11(n)(4)(I), and 13(e) of the Federal Deposit Insurance Act that to be enforceable against the FDIC, any agreement that tends to diminish or defeat the FDIC's interest in an asset must be executed contemporaneously with the acquisition of the asset by the institution (the "contemporaneous" requirement).

Pursuant to 12 U.S.C. 1821(e)(1), the FDIC, when acting as conservator or receiver of any insured depository institution, has the power to disaffirm or repudiate any contract or lease (i) to which the institution is a party; (ii) the performance of which the conservator or receiver, in the conservator's or receiver's discretion, determines to be burdensome; and (iii) the disaffirmance or repudiation of which the conservator or receiver determines, in the conservator's or receiver's discretion, will promote the orderly administration of the institution's affairs. Repudiation of a contract relieves the FDIC from performing any unperformed obligations remaining under the contract. Repudiation also entitles the other party to the contract to a claim for damages, which are limited by statute to actual direct compensatory damages determined as of the date of the appointment of the receiver or conservator. See 12 U.S.C. 1821(e)(3).

Pursuant to sections 11(d)(9), 11(n)(4)(I), and 13(e) of the Federal Deposit Insurance Act, no agreement that tends to diminish or defeat the FDIC's interest in an asset acquired from an insured depository institution is enforceable against the FDIC unless such agreement meets certain requirements. One of those requirements is that the agreement be executed by the depository institution and any person claiming an adverse interest thereunder contemporaneously with the acquisition of the asset by the institution.

In order for a transfer of financial assets by an insured depository institution in connection with a securitization or in the form of a participation to be accounted for as a sale, the proposed rule provides that the FDIC shall not, by exercise of its authority to disaffirm or repudiate contracts under 12 U.S.C. 1821(e), reclaim, recover, or recharacterize as property of the institution or the receivership any financial assets transferred by an insured depository institution in connection with a securitization or in the form of a participation. Although the repudiation of a securitization or participation will not affect transferred financial assets,

repudiation will excuse the FDIC from performing any continuing obligations imposed by the securitization or participation. If the FDIC, in order to terminate such continuing obligations or duties, seeks to disaffirm or repudiate an agreement or contract under which an insured depository institution has transferred financial assets in connection with a securitization or in the form of a participation, the FDIC will not seek to reclaim, recover, or recharacterize as property of the institution or the receivership such financial assets.

The proposed rule applies only to those securitizations or participations in which the transfer of financial assets meets all conditions for sale accounting treatment under generally accepted accounting principles, other than the "legal isolation" condition as it applies to institutions for which the FDIC may be appointed as conservator or receiver, which the proposed rule is intended to address.

As part of the definition of "participation," the proposed rule provides that a participation must be "without recourse," that is, the participation must not be subject to any agreement that requires the lead to repurchase the participant's interest or to otherwise compensate the participant upon the borrower's default on the underlying obligation. The term "without recourse" does not, however, preclude the lead institution from retaining a subordinated interest in the participated obligation, against which losses are initially allocated.

The proposed rule does not apply unless the insured depository institution received adequate consideration for the transfer of financial assets at the time of the transfer, and the documentation effecting the transfer of financial assets reflects the intent of the parties to treat the transaction as a sale, and not as a secured borrowing, for accounting purposes.

The proposed rule shall not be construed as waiving, limiting or otherwise affecting the rights or powers of the FDIC to take any action or to exercise any power not specifically limited by this section, including, but not limited to any rights, powers or remedies of the FDIC regarding transfers taken in contemplation of the institution's insolvency or with the intent to hinder, delay, or defraud the institution or the creditors of such institution, or that is a fraudulent transfer under applicable law.

The proposed rule further provides that the FDIC shall not seek to avoid an otherwise legally enforceable

securitization agreement or participation agreement executed by an insured depository institution solely because such agreement does not meet the "contemporaneous" requirement of sections 11(d)(9), 11(n)(4)(I), and 13(e) of the Federal Deposit Insurance Act.

The proposed rule is intended to apply to securitizations and participations that are engaged in by insured depository institutions while the rule is in effect, even if the rule is later repealed. Consequently, paragraph (g) provides that the rule will be effective unless repealed by the FDIC upon 30 days notice and opportunity for comment provided in the **Federal Register**, but in the event of such repeal, the rule shall continue to be effective with respect to any transfers made before the date of the repeal.

## II. Paperwork Reduction Act

No collection of information pursuant to section 3504(h) of the Paperwork Reduction Act (44 U.S.C. 3501 *et seq.*) is contained in the proposed rule. Consequently, no information was submitted to the Office of Management and Budget for review.

## III. Regulatory Flexibility Act

The proposed rule is consistent with the FDIC's current practice and does not represent a change in the law with respect to securitizations and participations. Pursuant to section 605(b) of the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*), it is certified that the proposed rule will not have a significant economic impact on a substantial number of small business entities.

## IV. The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The FDIC has determined that this proposed rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105-277, 112 Stat. 2681 (1998).

## List of Subjects in 12 CFR Part 360

Banks, banking, Savings associations.

For the reasons set out in the preamble, the FDIC Board of Directors proposes to amend 12 CFR part 360 as follows:

## PART 360—RESOLUTION AND RECEIVERSHIP RULES

1. The authority citation for part 360 is revised to read as follows:

**Authority:** 12 U.S.C. 1821(d)(1), 1821(d)(11), 1821(e)(1), 1821(e)(8)(D)(i),

1823(c)(4), 1823(e)(2); Sec. 401(h), Pub.L. 101-73, 103 Stat. 357.

2. Section 360.6 is added to part 360 to read as follows:

**§ 360.6 Treatment by the Federal Deposit Insurance Corporation as conservator or receiver of financial assets transferred in connection with a securitization or participation.**

(a) *Definitions.* (1) *Beneficial interest* means debt or equity (or mixed) interests or obligations of any type issued by a special purpose entity that entitle their holders to receive payments that depend primarily on the cash flow from financial assets owned by the special purpose entity.

(2) *Financial asset* means cash or a contract or instrument that conveys to one entity a contractual right to receive cash or another financial instrument from another entity.

(3) *Participation* means the transfer or assignment of an undivided interest in all or part of a loan or a lease from a seller, known as the "lead", to a buyer, known as the "participant", without recourse to the lead, pursuant to an agreement between the lead and the participant. *Without recourse* means that the participation is not subject to any agreement that requires the lead to repurchase the participant's interest or to otherwise compensate the participant upon the borrower's default on the underlying obligation.

(4) *Securitization* means the issuance by a special purpose entity of beneficial interests:

(i) The most senior class of which at time of issuance is rated in one of the four highest categories assigned to long-term debt or in an equivalent short-term category (within either of which there may be sub-categories or gradations indicating relative standing) by one or more nationally recognized statistical rating organizations; or

(ii) Which are sold in transactions by an issuer not involving any public offering for purposes of section 4 of the Securities Act of 1933, as amended, or in transactions exempt from registration under such Act pursuant to Regulation S thereunder (or any successor regulation).

(5) *Special purpose entity* means a trust, corporation, or other entity with a distinct standing at law separate from the insured depository institution that is primarily engaged in acquiring and holding (or transferring to another special purpose entity) financial assets, and in activities related or incidental thereto, in connection with the issuance by such special purpose entity (or by another special purpose entity that acquires financial assets directly or

indirectly from such special purpose entity) of beneficial interests.

(b) The FDIC shall not, by exercise of its authority to disaffirm or repudiate contracts under 12 U.S.C. 1821(e), reclaim, recover, or recharacterize as property of the institution or the receivership any financial assets transferred by an insured depository institution in connection with a securitization or participation, provided that such transfer meets all conditions for sale accounting treatment under generally accepted accounting principles, other than the "legal isolation" condition as it applies to institutions for which the FDIC may be appointed as conservator or receiver, which is addressed by this section.

(c) Paragraph (b) of this section shall not apply unless the insured depository institution received adequate consideration for the transfer of financial assets at the time of the transfer, and the documentation effecting the transfer of financial assets reflects the intent of the parties to treat the transaction as a sale, and not as a secured borrowing, for accounting purposes.

(d) Paragraph (b) of this section shall not be construed as waiving, limiting, or otherwise affecting the power of the FDIC, as conservator or receiver, to disaffirm or repudiate any agreement imposing continuing obligations or duties upon the insured depository institution in conservatorship or receivership.

(e) Paragraph (b) of this section shall not be construed as waiving, limiting or otherwise affecting the rights or powers of the FDIC to take any action or to exercise any power not specifically limited by this section, including, but not limited to, any rights, powers or remedies of the FDIC regarding transfers taken in contemplation of the institution's insolvency or with the intent to hinder, delay, or defraud the institution or the creditors of such institution, or that is a fraudulent transfer under applicable law.

(f) The FDIC shall not seek to avoid an otherwise legally enforceable securitization agreement or participation agreement executed by an insured depository institution solely because such agreement does not meet the "contemporaneous" requirement of sections 11(d)(9), 11(n)(4)(I), and 13(e) of the Federal Deposit Insurance Act.

(g) This section may be repealed by the FDIC upon 30 days notice and opportunity for comment provided in the **Federal Register**, but in the event of such repeal, the section shall continue to be effective with respect to any

transfers made before the date of the repeal.

By order of the Board of Directors.

Dated at Washington, DC this 31st day of August, 1999.

Federal Deposit Insurance Corporation.

**Robert E. Feldman,**

*Executive Secretary.*

[FR Doc. 99-23384 Filed 9-8-99; 8:45 am]

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## ENVIRONMENTAL PROTECTION AGENCY

### 40 CFR Part 52

[Region 2 Docket No. NJ35-2-196; FRL-6434-1]

#### Approval and Promulgation of Air Quality Implementation Plans; New Jersey; Approval of Carbon Monoxide State Implementation Plan Revision; Determination of Carbon Monoxide Attainment

**AGENCY:** Environmental Protection Agency (EPA).

**ACTION:** Proposed rule.

**SUMMARY:** In today's action, the EPA is determining that the New York-Northern New Jersey-Long Island carbon monoxide nonattainment area has attained the carbon monoxide National Ambient Air Quality Standards. As a consequence of this determination, EPA is proposing to approve a State Implementation Plan revision submitted by the State of New Jersey on August 7, 1998. That revision removes New Jersey's oxygenated gasoline program as a carbon monoxide control measure from the State's SIP.

**DATES:** Comments must be received on or before October 12, 1999.

**ADDRESSES:** All comments should be addressed to: Raymond Werner, Acting Chief, Air Programs Branch, Environmental Protection Agency, Region 2, 290 Broadway, 25th Floor, New York, NY 10007-1866.

Copies of the State submittal and EPA's technical support document are available for public inspection during normal business hours, by appointment, at the following addresses:

Environmental Protection Agency, Region 2, Air Programs Branch, 290 Broadway, 25th Floor, New York, NY 10007-1866.

New Jersey Department of Environmental Protection, Bureau of Air Quality Planning, 401 East State Street, CN027, Trenton, New Jersey 08625.

**FOR FURTHER INFORMATION CONTACT:** Michael P. Moltzen, Air Programs