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News Bulletin

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Insurance Companies Adopt Thrift Holding Company Structure to Become Eligible for Treasury Capital Purchase Program and FDIC Liquidity Guarantee

On November 14, the deadline for financial institutions to file an application for the Department of the Treasury's Capital Purchase Program (the "CaPP"), as authorized under the Emergency Economic Stabilization Act of 2008 (EESA), four large insurance companies announced proposed acquisitions of distressed thrifts. Hartford Financial Services Group acquired Federal Trust Corporation, which had been ordered by the Office of Thrift Supervision (the "OTS") to find a buyer by November 15. The acquisition is contingent upon Hartford being able to secure approval to participate in the CaPP. Hartford has agreed that, if the acquisition is finalized, it would inject a significant amount of capital into the thrift. In addition, Genworth Financial agreed in principle to acquire Inter Savings Bank while Lincoln National Corp. will acquire Newton County Savings Bank. Similarly, Aegon NV's U.S. subsidiary, Transamerica Corp., will acquire Suburban Federal Savings and Loan. Each of these insurers filed an application to participate in the CaPP. In addition, Phoenix Cos., a life and annuity insurer, filed a "placeholder" application with the OTS prior to the deadline, indicating that it would like to acquire a thrift in order to participate in the CaPP, but has not yet worked out the details of doing so.

As thrift holding companies, the insurance companies became eligible to apply to receive capital infusions under the CaPP and also to participate in the FDIC's Temporary Liquidity Guarantee Program (the "TLGP").

By acquiring a thrift institution and filing an application to become a thrift holding company, these insurance companies become "eligible institutions" under the TLGP. The TLGP is open to FDIC-insured depository institutions (banks and thrifts), U.S. bank holding companies (BHCs), U.S. financial holding companies, and U.S. thrift holding companies that engage in activities that are permissible for financial holding companies under Section 4(k) of the Bank Holding Company Act (which excludes primarily commercial activities). Affiliates of insured depository institutions also may participate, upon application to, and acceptance by, the FDIC in consultation with the institution's primary federal banking regulator.

The TLGP consists of two basic components: a temporary guarantee of newly issued senior unsecured debt (the "Debt Guarantee Program") and a temporary unlimited guarantee of funds in noninterest-bearing transaction accounts at FDIC-insured institutions (the "Transaction Account Guarantee Program"). Under the Debt Guarantee Program, the FDIC guarantees senior unsecured debt newly issued by an eligible institution. The maximum guaranteed amount is 125 percent of the par or face value of senior unsecured debt outstanding as of September 30, 2008 that is scheduled to mature by June 30, 2009. The guarantee will remain in place until the earlier of the debt's maturity or June 30, 2012. Under the Transaction Account Guarantee Program, the FDIC provides an unlimited guarantee until December 31, 2009 of all funds, regardless of amount, held in noninterest-bearing transaction accounts.

Both guarantees initially are automatic; however, eligible institutions must notify the FDIC by December 5, 2008 whether they wish to opt out of the programs. All commonly controlled institutions must make the same decision. By choosing to remain in the programs, participants, including the newly-eligible insurance companies, will be able to take advantage of the guarantees until the programs terminate, subject to payment of the applicable fees to the FDIC in exchange for the coverage.

In addition, through the CaPP, in light of their new status as thrift holding companies, insurers will be eligible to apply to receive infusions of capital from Treasury equal to 1% to 3% of their risk-weighted assets. To qualify for the CaPP, an institution must be an FDIC-insured depository institution which includes U.S. banks and savings associations not controlled by a BHC or thrift holding company, U.S. BHCs and U.S. thrift holding companies that are engaged predominately in Section 4(k) activities under the Bank Holding Company Act (BHCA), or whose depository institution subsidiaries are the subject of an application under Section 4(c)(8) of the BHCA. These capital injections will take the form of shares of preferred stock and warrants to purchase common stock. In connection with such infusions, the insurers also will be subject to the executive compensation and other limitations associated with the CaPP.

For insurance companies, becoming a thrift holding company, even in order to access the EESA programs, will have certain potentially negative consequences that need to be considered. Conversion subjects the insurers and their non-thrift subsidiaries to regulation by the OTS, and limits the activities in which the insurers may participate. Moreover, inter-affiliate transactions will be constrained under applicable banking law, under a different and more rigorous regime than inter-affiliate transactions under applicable insurance law. As a result of their holding company status, the insurance companies and their non-thrift insurance subsidiaries will be subject to dual regulation by the OTS and state insurance commissioners.

Even prior to these decisions to convert to thrift holding company structure, several other insurance companies were already members of organizations that were financial holding companies, subject to federal regulation. Financial holding companies are a type of BHC that, in addition to the activities permitted for BHCs, can engage, through their affiliates, in certain enumerated financial activities, including insurance. In addition, many insurance companies already hold savings and loans as subsidiaries, again, subjecting them to additional regulation. Considering this, there should be considerable experience with this dual regulation and it is unlikely to raise significant conflicts.

The recent decisions by insurance companies to adopt thrift holding company structures in order to become eligible for federal assistance follows the determination of several other companies to adopt BHC structures for the same or similar purposes--the most recent of which was American Express. The recent federal bailout of American International Group and the conversion of Goldman Sachs and Morgan Stanley (each of which have insurance company subsidiaries) to BHCs have expanded the numbers of insurance company organizations subject to the consequent regulation by a federal regulator, such as the OTS or the Federal Reserve. Although there is no direct regulation of the insurance operations of such institutions, exposure to these regulators may ease concerns over federal oversight of insurance in place of traditional state insurance regulation. Familiarity with federal regulation also may strengthen calls for a consolidated form of federal insurance regulation. In addition to centralized information-sharing, such proposals include the issuance of optional federal charters to insurers. Generally, insurance industry trade associations representing large multi-state insurance companies favor such an approach, although state insurance regulators, concerned that a federal regulator would not be in a position to monitor consumer protection in a targeted fashion, oppose such suggestions. Thus, although regulation by federal bank regulators will not resolve the efficacy of uniform insurance regulation across state boundaries, proponents are likely to seize upon the economic and financial factors underlying these conversions to federally regulated status and any positive experience under such regimes as additional support for consolidated regulation.

Additional Information

For additional information on the FDIC's TLGP or related developments, please see our dedicated webpage at http://www.mofo.com/news/updates/files/14605.html.

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