

FINANCIAL INSTITUTION BANKRUPTCY ACT OF 2017 – BIG CHANGES FOR BIG BANKS

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When the real estate market and financial markets tumbled during 2007-2008, the fallout was felt by financial institutions from large multi-billion dollar banks to small Community Banks. As these banks struggled to stay alive, a trend emerged for bank holding companies to market and sell a distressed bank through Section 363 of the Bankruptcy Code. This alternative was utilized in many instances as opposed to a traditional "reorganization plan" or takeover by the FDIC. This process oftentimes allowed for a prompt sale of the bank assets, allowed the bank to remain open and likely resulted in the best possible outcome for all constituencies rather than an FDIC takeover or bank failure.

While the Section 363 sale process did move quickly, many commentators recognized that for larger financial institutions, even that process could take too long. In response, on April 5, 2017, the U.S. House of Representatives passed the Financial Institution Bankruptcy Act of 2017 (the "FIBA"). FIBA allows financial institutions that have over \$50 billion in assets to elect a new "Subchapter V" bankruptcy process. The purpose of the Subsection V is to allow the qualifying financial institution to transfer the distressed bank's assets to a newly formed bridge company which would be subject to specific guidelines and a trust agreement specific to the entity which would govern the terms of the process. The Bankruptcy Court could order such a transfer only after it was determined, inter alia, that the transfer is necessary to prevent serious adverse effects on financial stability in the United States and the transfer does not provide for the assumption of any capital structure debt (i.e. the stock of the distressed financial institution would not hold equity in the bridge company.) The transfer could occur after a hearing not less than 24 hours after the bankruptcy petition is filed with the Bankruptcy Court (i.e. the transfer could arguably take place over a weekend, if the filing took place on a Friday, to minimize disruption to a bank's customers). A special trustee would be appointed by the Bankruptcy Court to oversee the bridge company. The Bankruptcy Judges overseeing such cases will be selected randomly from a panel of judges designated by the Chief Justice of the United States Supreme Court.

FIBA radically changes certain fundamental provisions of the Bankruptcy Code for the sole benefit of large financial institutions. It will be worth watching to see when and if any banks begin to utilize these special provisions of the Bankruptcy Code and the evolution of the interpretation of FIBA.

For more information, please contact the author, Brian Rich, on our Business Reorganization Team.

Topics

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