



February 27, 2012

David Baris, Esq.  
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American Association of Bank Directors  
1250 24<sup>th</sup> Street, NW, Suite 700  
Washington, D.C. 20037

Re: Your Letter of February 3, 2012

Dear Mr. Baris:

Thank you for your recent letter of February 3, 2012. I appreciate the opportunity provided in responding to your letter to clarify an issue that, as your letter reflects, may be giving rise to misperceptions. In your letter, you argue that Part 359 of the FDIC's regulations (12 C.F.R. Part 359) does not prohibit a bank's insurance policy from covering civil money penalties (CMPs) against institution-affiliated parties (IAPs). Your contention flows from your conclusion that Part 359 does not apply unless the insured depository institution itself makes the prohibited indemnification payment or pays for insurance that covers CMPs or judgments obtained by the federal banking agency. As a result, you argue that where the insurance is procured by the institution and provides for reimbursement for IAPs for CMPs or judgments obtained by federal banking agency, but the IAPs pay for this portion of the coverage, there is no prohibited indemnification payment. For the reasons explained below, your interpretation of Part 359 is incorrect.

Part 359 embodies an important public policy designed to ensure that CMPs obtained by bank regulatory agencies against IAPs will serve as a deterrent to conduct that is inimical to the safe and sound operation of insured institutions. This was made clear when Part 359 was adopted in 1996. In the Preamble, the FDIC stated that one of the purposes of Part 359 is "making sure that [IAPs] are held accountable for substantive violations of law or regulation." 61 Fed. Reg. 5926, 5929 (February 15, 1996). This purpose would not be served by allowing insured depository institutions to purchase CMP coverage for IAPs through "endorsements" to the institution's insurance policy (regardless of whether the institution is reimbursed for the designated cost of the "endorsement"). As a result, Part 359 makes clear that insured institutions cannot act to protect their IAPs from the potential consequences of individual conduct that gives rise to a CMP against that individual.

Part 359 does so, in part, by broadly prohibiting an insured institution or holding company from making a “prohibited indemnification payment.” *See* 12 C.F.R. § 359.3. The term “prohibited indemnification payment” is defined as follows:

The term *prohibited indemnification payment* means any payment (or any agreement or arrangement to make any payment) by any insured depository institution or an affiliated depository institution holding company for the benefit of any person who is or was an IAP of such insured depository institution or holding company, to pay or reimburse such person for any civil money penalty or judgment resulting from any administrative or civil action instituted by any federal banking agency, or any other liability or legal expense with regard to any administrative proceeding or civil action instituted by any federal banking agency which results in a final order or settlement pursuant to which such person:

- (i) Is assessed a civil money penalty;
- (ii) Is removed from office or prohibited from participating in the conduct of the affairs of the insured depository institution; or
- (iii) Is required to cease and desist from or take any affirmative action described in section 8(b) of the Act with respect to such institution.

12 C.F.R. § 359.1(l)(1). *See also* 12 U.S.C. § 1828(k)(5).

The focus on payments by the insured institution in this definition is understandable given the overall context of Part 359 and its focus on golden parachute payments and indemnification payments. Part 359.1(l)(2) does recognize that insurance may be appropriate to cover legal fees and related expenses as well as restitution payments for losses to the insured institution. Such coverage principally protects the insured institution from the financial consequences of wrongful conduct by its IAPs and, consequently, is consistent with well-settled public policy. However, Part 359 plainly prohibits the insured institution from making “any agreement or arrangement to make any payment” to reimburse the IAP for a CMP.

As a result, it is clear that Part 359 prohibits both a direct payment as well “any agreement or arrangement” to pay or reimburse an IAP for the cost of CMPs obtained by the federal banking agency. 12 C.F.R. § 359.1(l)(1). Nothing in Part 359.1(l)(2) can be read to the contrary. In fact, it underscores the overall focus of Part 359 on ensuring that IAPs will owe their fealty and expertise to the insured institution and will not be protected from the consequences of their actions that may be contrary to that responsibility.

Given this public policy, and the terms of Part 359, the fact that the portion of the premium of an insurance policy procured by the insured institution that is attributable to an “endorsement” protecting IAPs from CMPs is paid by the IAP does not make it permissible. The CMP “endorsement” is part of the insurance policy purchased by the insured institution. The contracting parties to this policy are the insurance company and the insured institution. Thus, the party procuring the insurance policy – including the CMP “endorsement” – is the insured depository institution.

David Baris, Esq.  
February 27, 2012  
Page 3

Under Part 359, an insured institution simply cannot purchase an insurance policy with CMP coverage for IAPs. No exception exists under Part 359 for cases in which the insured institution purchases an impermissible insurance policy but then collects reimbursement from the IAP for some portion of the institution's insurance premiums.

For the reasons explained above, it is my view that your interpretation of Part 359 is in error. An insured depository institution or holding company cannot purchase CMP coverage for IAPs under Part 359, even if the IAP offers to reimburse the depository institution for the designated cost of a CMP "endorsement."

Sincerely,

A handwritten signature in black ink, reading "Michael H. Krimminger". The signature is written in a cursive, flowing style.

Michael H. Krimminger

General Counsel  
Federal Deposit Insurance Corporation