Attachment A

BRIEF SUMMARY OF THE DEVELOPMENT OF THE D'OENCH DOCTRINE

In an effort to protect the federal deposit insurance funds and the innocent depositors and creditors of insured financial institutions, the courts fashioned a judge-made rule that bars a party who fails to fully document or record an agreement with a bank from relying on that agreement to assert a claim against a failed bank, or to avoid payment of a debt owed to the bank. The courts phrased the test in terms of the failure to fully document or record the agreement as creating an arrangement that would tend to mislead the banking authorities because the arrangement would be secret.

The classic case is a borrower who signs a written loan agreement, but later claims that he or she had an unwritten promise from the bank that repayment could be on terms different from those reflected in the loan file or deferred completely, or that the bank would provide some additional services or "sweetener" not contained in the loan documents. If enforceable, this secret agreement could render an apparently valuable asset worthless or create hidden liabilities that would mislead regulators and the receiver in their efforts to accurately determine the value of a bank's assets and liabilities.

The United States Supreme Court adopted and extended these principles in D'Oench, Duhme & Co. v. FDIC, 315 U.S. 447 (1942). In D'Oench, the FDIC brought an action to enforce payment of a promissory note which it had acquired from a failed institution. As a defense to the action, the borrower claimed that it was not liable because the notes were given pursuant to an undocumented agreement that the notes would not be called for payment. The borrower raised the secret agreement and failure of consideration as defenses to the FDIC's action. The United States Supreme Court held that the secret agreement could not be a defense to a suit by the FDIC because, by simply entering into that agreement, the borrower facilitated creation of a transaction that could mislead the banking authorities. The Court refused to require intent to defraud by the borrower or claimant because the public policy purpose of requiring records in the bank's files would not be served by limiting the doctrine only to those cases.

ENACTMENT OF SECTION 1823(e)

Congress first enacted Section 1823(e) in 1950. Section 1823(e) currently imposes four requirements for an agreement to be enforceable against the bank receiver:

(1) The agreement must be in writing.
(2) The agreement must be executed by the bank and any person claiming under it contemporaneously with the acquisition

of the asset by the bank, which generally means the closing on the loan.

(3) The agreement must be approved by the board of directors or loan committee and reflected in the appropriate minutes.

(4) The agreement must be continuously an official record of the bank.

Effectively, this section bars any claim or defense to an agreement with the bank that is based on facts outside the documents contained in the institution's files. Like the D'Oench doctrine, section 1823(e) is designed to protect the federal banking regulatory authorities from undocumented agreements that impede the regulatory authorities' ability to perform their congressionally mandated functions.

Section 1823(e) was enacted to clarify and to provide the public with notice of the requirements for enforceable agreements. In particular, while D'Oench and later court decisions had involved debtors who had lent themselves to questionable arrangements, there was uncertainty as to the enforceability against the FDIC of "good faith" unrecorded side agreements. In fact, the final version of section 1823(e) was enacted because Congress concluded that simply limiting the statute to cases where the borrower or claimant committed fraud would not serve the goal of insuring reliable bank examinations and immediate availability of depositor funds through prompt resolutions of failed banks.

The Congressional debates leading to the enactment of section 1823(e) mirror many of the concerns expressed in the current debate. It is clear that the statute was intended to provide the FDIC with additional assurance that it could rely on bank records. As recently as 1987, Justice Scalia, speaking for a unanimous Supreme Court, stated in Langley v. FDIC, 484 U.S. 86 (1987):

> [O]ne purpose of § 1823(e) is to allow federal and state bank examiners to rely on a bank's assets . . . Neither the FDIC nor state banking authorities would be able to make reliable evaluations if bank records contained seemingly unqualified notes that are in fact subject to undisclosed conditions.
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> A second purpose of § 1823(e) is implicit in its requirement that the "agreement" not merely be on file in the bank's records at the time of an examination, but also have been executed and become a bank record "contemporaneously" with the making of the note and have been approved by officially recorded action of the bank's board or loan committee. These latter requirements ensure mature consideration of unusual loan transactions by senior bank officials, and

prevent fraudulent insertion of new terms, with the collusion of bank employees, when a bank appears headed for failure.

The issue of whether the D'Oench doctrine and section 1823(e) should be limited solely to cases of fraudulent schemes was apparently first brought to Congress's attention by Representative Frances E. Walter, a member of the House Judiciary Committee in 1949. One of Rep. Walter's constituents, Mr. Alker, had lost a case against the FDIC on the ground that D'Oench prevented use of certain oral agreements, even though he claimed that he had not participated in any deceptive scheme or arrangement.

Rep. Walter introduced a bill that, in addition to amending certain provisions of the criminal code, would have subjected the FDIC as receiver for a failed bank to any defense that could have been raised against the open bank, unless the borrower or claimant committed actual fraud. The bill would have been retroactive to 1933 and, hence, to Mr. Alker's case.

Hearings on the bill were held on August 10, 1949, and on June 12, 1950. The FDIC opposed the bill because it "would encourage secret agreements between a bank and its debtors, which conceivably might be short of actual fraud, to the detriment not only of [the FDIC], but also of general creditors and uninsured depositors." The FDIC explained that insured banks:

> are examined by governmental authorities which in turn publish reports and statistics concerning their condition. All of such reports are intended to be and are relied upon by the public generally. This reliance of necessity is based upon what records of the bank disclose and the public invests or deposits its money accordingly. Even the most fundamental principles of honesty, aside from any technical rules governing distribution of property of an insolvent bank, require that these creditors be protected against any arrangements, understandings, or agreements which are not disclosed in the records of the banks and, therefore, would not be reflected in these reports.

The bill was also opposed by the Departments of Justice and Treasury, the Federal Reserve Board and the National Association of Supervisors of State Banks.

Other witnesses and members of the Committee repeatedly expressed similar concerns about the bill and stressed the importance of the FDIC's ability to rely on the written records of the bank as well as the minimal burden a writing requirement would have on banks and their customers. One bank president testified:

> [T]he bank examiner is a representative of the public, and he has a right to rely on [the note], and I do not care whether he is an examiner for the FDIC, whether he is an examiner for the Comptroller's Office, or whether he is an examiner for one of the State Departments, I do not care who he is representing, he is still representing the American public and he has a right to know that within the four corners of the note that is all there is, that there is no more.

Rep. Walter's bill never left the Judiciary Committee.

On June 20, 1950, one week after the second of the hearings on H.R. 5811, the House Banking and Currency Committee held hearings on S. 2822, which was to become the FDI Act. Although S. 2822 as introduced contained no provision concerning the protection of the FDIC against unrecorded agreement, Rep. Multer, referring to the recent Judiciary Committee hearings, raised the issue in a question to FDIC Director Cook:

> Mr. Multer: There has been considerable litigation through the years during the existence of the Corporation in which contentions have been made that agreements between the banks and debtors have not been lived up to after the banks were closed down and that the FDIC, in collecting the assets of the bank, was put in a more favorable position than the bank itself would have been and that the FDIC could ignore the agreements with the debtors. I think some legislation has been introduced in a hearing held before another committee of the House on the subject. Can you tell us briefly whether or not there is any objection to putting into this proposed law an amendment to require the FDIC to comply with any such agreements that have been made in good faith and which are properly recorded between the debtors and the banks closed up, or taken over, or merged?
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> Mr. Cook: I think that statement of yours covered the ground entirely -- where you are properly supported by such agreements and not dependent upon oral agreements that have no binding effect. If the bars are once let down on that, there would not be a safe bank in the United States today, because anybody could claim that so-and-so had happened and there would be no evidence to support it. . . .
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> Mr. Multer: I think the policy of your bank is to honor any such bona fide agreement.
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> Mr. Cook: We never back away from a bona fide agreement and when the record is clear we inherit that obligation and stand by it. We cannot be bound when there is no record.

The bill that the Banking Committee reported to the House contained the provision that has become Section 1823(e). The provision went beyond the ideas expressed in the Judiciary Committee hearings by opponents of Rep. Walter's bill and required more than merely a writing to support variations from the text of written obligations. It also required that such side agreements be executed by the bank and the debtor simultaneously with the execution of the note, that it have been continuously an official record of the bank, and that official minutes show that it was approved by the bank's board of directors or loan committee. With one minor change in language, the Committee provision became law.

As finally enacted, section 1823(e) strikes a careful balance between protection of borrowers and protection of depositors and bank creditors nationwide. On the one hand, it precisely delineates the means by which borrowers can protect themselves; on the other hand, it enables the FDIC to rely on the bank's records when assessing the true condition of FDIC-insured banks and when collecting on obligations owing to a failed bank.