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Regulatory Update

Nonbanks and Failed Bank Acquisitions: A Playbook for Participation Becomes Clearer

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Participating in the resolution of failing banks in the U.S. has presented a frustrating paradox for private equity and other nonbank corporate investors: attractive targets, but limited ability to act. The Federal Deposit Insurance Corporation (FDIC) removed one constraint by rescinding its *Statement of Policy on Qualifications for Failed Bank Acquisitions* (the Policy Statement) on March 19. The rescission of the Policy Statement signals an openness by the FDIC to nonbank companies' participation in failed bank transactions, including the acquisition of loan portfolios and, potentially, whole-bank acquisitions.

The rescission follows FDIC Chairman Travis Hill previewing the possibility of an “emergency exception that would enable a nonbank to rapidly set up a shelf charter to bid on a failed institution following a sudden failure” and the development of a pre-qualification process for nonbank bidders, “with the intent of qualifying nonbank bidders in advance of any offering.” The pre-failure qualification process and application are expected to be released following the completion of a pilot program that began in January of this year.

Through these actions, the prospect of participating in failed bank auctions may become more attractive to — and realistic for — private equity and other nonbank bidders. Of course, the Bank Holding Company Act (BHCA) administered by the Board of Governors of the Federal Reserve System (Federal Reserve) and other relevant statutes still apply and will need to be carefully considered by any investor who participates in a failed bank auction.

1. The Core Change: Removing Barriers to Entry

The Policy Statement imposed a set of constraints that made failed-bank acquisitions unattractive and challenging for nonbank investors: high capital standards above the regulatory minimum requirements, forced holding periods, prohibitions on transactions with affiliates and certain portfolio companies exceeding typical regulatory restrictions, and a ban on “complex and functionally opaque” ownership structures. The rescission removes these deterrents from potential nonbank acquirers and permits nonbank bidders to meet the same regulatory requirements as chartered banks to acquire on a failed institution rather than having to exceed them.

2. The Economics Were Not the Problem

From a financial returns perspective, failed-bank transactions have always been compelling because:

- The acquirer purchases discounted assets with immediate mark-to-market upside.

- Possible loss-sharing structures could shift downside risk to the FDIC.
- The possibility of “seller financing” (i.e., FDIC financing) at a favorable interest rate allows buyers to enhance leverage and returns.

In most distressed asset classes, these features would attract significant capital. Historically, participation has been constrained not by economics, but by structure.

That distinction matters. When access improves in a market where the underlying return profile is already attractive, capital tends to move quickly. Moreover, and perhaps a driving force for the recession, competition in bidding for failed banks should raise the value of bids to the FDIC and thus reduce the cost of a resolution.

3. The Constraint That Still Matters: Bank Holding Company Act and ‘Control’

Despite these changes, one significant limitation remains: Controlling a bank is not the same as owning any other type of financial asset. This is mainly due to the BHCA, which limits corporate ownership of banks. Under the BHCA and its implementing regulations, any company that controls a bank (or an intermediate company) is considered a bank holding company (BHC) subject to regulation, supervision and examination by the Federal Reserve. The prospect of complying with the BHCA, which the Policy Statement recession does not modify, remains an onerous hurdle for nonbank bidders. In practice, this has led to:

- Consortium or “club” deals to stay below control thresholds established by statute and regulation.
- Asset-focused strategies rather than whole-bank acquisitions.
- Complex governance structures to navigate regulatory boundaries.

4. Shelf Charters: A Mechanism to Pursue Whole Bank Deals

Only banks can participate in whole-bank acquisitions because only banks can assume insured deposits. To encourage nonbank participation in the failed bank auction process during the Great Financial Crisis of 2008–11, the U.S. banking agencies established a process whereby a nonbank investor could seek preliminary regulatory clearance to organize a new bank to acquire a whole bank that has failed. Such a preliminary charter is known as a “shelf” charter, so called because it “sits on the shelf” until it is activated for use following a successful bid on a failed bank. A shelf charter is granted by the Office of the Comptroller of the Currency (OCC) or relevant state licensing authority following review of the applicant’s capital plan, proposed board and executive officers, and business plan. This preliminary review is only the first step — a shelf charter requires final approval of a specific transaction by the licensing agency, approval of FDIC insurance and, potentially, approval by the Federal Reserve as part of a bank holding company application.

The shelf charter has not been a widely adopted vehicle to facilitate nonbank participation in failed bank acquisitions. In 2023, the OCC approved a shelf charter for Porticoes National Bank — the first approval since 2010. While some thought the conditional approval of Porticoes National Bank portended a rush of shelf charter applications, none followed.

However, following the recession of the Policy Statement, nonbank participation has become more attractive, and a shelf charter allows a potential nonbank acquirer to quickly act in the event a bank fails and the nonbank acquirer has an interest in acquiring the whole bank. Chairman Hill has stated that the FDIC is working on a proposal to facilitate a speedy review of a deposit insurance application by an entity with a shelf charter, as well as an interagency policy that would address the chartering, deposit insurance application and bank holding company application processes for shelf charters. If these proposals come to fruition, a nonbank bidder’s path to a bank charter may be further streamlined.

Of course, the BHCA remains an important consideration that nonbank investors will need to carefully consider when structuring a specific transaction.

Conclusion

For years, nonbanks, including private equity funds, have been constrained from participating in failed bank auctions by regulatory conditions, not opportunity. Recent FDIC actions are making it easier for nonbanks to participate in failed bank auctions, and future actions may make participation easier still. For companies interested in whole-bank acquisitions, shelf charters provide a path to participation, which is especially critical when speed is important. To participate, firms should begin developing their failed bank acquisition strategies now, rather than waiting until a failed bank auction begins.

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