



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 29, 2008

H. Rodgin Cohen, Esq.
Sullivan & Cromwell LLP
125 Broad Street
New York, New York 10004-2498

Dear Mr. Cohen:

This is in response to the request by Wachovia Bank, National Association (“Bank”), Charlotte, North Carolina, for an exemption from section 23A of the Federal Reserve Act and the Board’s Regulation W to allow Bank to purchase up to \$7 billion of auction-rate securities (“ARS”) from an affiliate.

Bank’s proposal to purchase ARS from its affiliate largely arises out of ongoing dislocations in the ARS market. Principally as a result of the ongoing turmoil in the financial markets, ARS auction failures became endemic in early 2008, and ARS became largely illiquid. ARS were often sold to customers seeking liquid investments for short-term needs. Many investors alleged that the brokerage firms that sold them ARS represented that ARS were essentially cash equivalents, and class-action lawsuits and lawsuits by state attorneys general were initiated against some brokerage firms. In addition, the Securities and Exchange Commission and some state securities regulators opened investigations into ARS sales practices.

Like many broker-dealers active in the ARS market, Wachovia Securities, LLC and Wachovia Capital Markets, LLC (collectively, “Wachovia Securities”) entered into agreements with the Securities and Exchange Commission and various state authorities to repurchase at par all ARS purchased by investors through Wachovia Securities before February 14, 2008. Pursuant to these agreements, Wachovia Securities agreed to purchase ARS from investors in three tranches between August 2008 and June 2009.

Wachovia Securities purchased \$1.43 billion of municipal auction-rate securities (“MARS”) from investors in August and September, []. Bank seeks an exemption from section 23A and Regulation W to enable Bank to purchase all MARS, student loan auction-rate securities (“SLARS”), and auction-rate preferred securities (“ARPS”) that are purchased by Wachovia Securities pursuant to the settlement agreements, including MARS already purchased by Wachovia Securities [] (collectively, “Eligible ARS”).

Section 23A and Regulation W limit the aggregate amount of “covered transactions” between a bank and any single affiliate to 10 percent of the bank's capital stock and surplus, and limit the aggregate amount of covered transactions between a bank and all its affiliates to 20 percent of the bank's capital stock and surplus.¹ “Covered transactions” include the purchase of assets by a bank from an affiliate, the extension of credit by a bank to an affiliate, the issuance of a guarantee by a bank on behalf of an affiliate, and certain other transactions.² The statute and regulation also require a bank to secure its extensions of credit to, and guarantees on behalf of, affiliates with prescribed amounts of collateral.³

The purchases of Eligible ARS by Bank from Wachovia Securities are covered transactions under section 23A and Regulation W. Wachovia Securities is an affiliate of Bank for purposes of section 23A and Regulation W because Wachovia Securities is indirectly controlled by Bank’s parent companies, Wachovia Corporation (“Wachovia”), Charlotte, North Carolina, and Wells Fargo & Company (“WFC”), San Francisco, California.⁴

The aggregate amount of the covered transactions is up to approximately \$7 billion, the Bank’s estimated purchase price for the Eligible

¹ 12 U.S.C. § 371c(a)(1) and 12 CFR 223.11 and 223.12.

² 12 U.S.C. § 371c(b)(7) and 12 CFR 223.3(h).

³ 12 U.S.C. § 371c(c) and 12 CFR 223.14.

⁴ On October 3, 2008, WFC entered into an agreement to acquire Wachovia. This transaction was approved by the Board on October 12, 2008. On October 20, 2008, WFC acquired approximately 39.9 percent of the voting stock of Wachovia.

ARS.⁵ This amount exceeds Bank's quantitative limits under the statute and rule.⁶ Accordingly, Bank is requesting an exemption from the quantitative limits of section 23A and Regulation W in connection with its purchase of assets from Wachovia Securities. Section 23A and Regulation W specifically authorize the Board to exempt transactions or relationships from the requirements of the statute and rule if the Board finds such an exemption to be in the public interest and consistent with the purposes of section 23A.⁷ The Board previously has indicated that the twin purposes of section 23A are (i) to protect against a depository institution suffering losses in transactions with affiliates and (ii) to limit the ability of an institution to transfer to its affiliates the subsidy arising from the institution's access to the federal safety net.⁸

Bank believes that granting the requested exemption would have public benefits because it would facilitate the provision of liquidity by Wachovia to customers holding unexpectedly illiquid securities as a result of dislocations in the ARS market.

The exemption would be subject to the following limits and conditions, which are designed to protect the safety and soundness of Bank in connection with the proposed transactions:

⁵ Bank proposes to purchase \$540 million in MARS held by Wachovia Securities. In addition, Wachovia Securities estimates that it will have to repurchase from investors up to \$4.2 billion of ARPS and \$1.2 billion of SLARS, which would in turn be purchased by Bank. The total potential amount of ARS repurchases by Wachovia Securities is approximately \$10 billion. The exemption request is limited to \$7 billion, which provides a cushion of \$1.1 billion over the expected repurchase amount.

⁶ As of September 30, 2008, Bank's capital stock and surplus was \$64.78 billion. Accordingly, for purposes of section 23A and Regulation W, the 10 percent limit for covered transactions with a single affiliate would be \$6.478 billion, and the 20 percent limit on covered transactions with all affiliates in the aggregate would be \$12.96 billion.

⁷ 12 U.S.C. § 371c(f)(2) and 12 CFR 223.43.

⁸ 67 Federal Register 76560 (Dec. 12, 2002).

- Bank's purchases of Eligible ARS from Wachovia Securities is limited to an aggregate amount of \$7.0 billion, which represents approximately 11 percent of the bank's capital stock and surplus.
- All Eligible ARS purchased by Bank must be externally rated investment grade by a nationally recognized statistical rating organization ("NRSRO"), and a majority of the Eligible ARS purchased by Bank must be rated in one of the two highest investment grade rating categories by an NRSRO.
- Bank must purchase the Eligible ARS at fair market value.
- Bank and Wachovia must enter into an irrevocable agreement pursuant to which Bank would have the right to sell the Eligible ARS to Wachovia by July 31, 2010 ("Repurchase Agreement"), at the price paid by the bank for the Eligible ARS plus any accrued but unpaid interest.
- Bank must exercise its right under the Repurchase Agreement no later than July 31, 2010.
- Wachovia must agree to repurchase from Bank, on a quarterly basis, any Eligible ARS that become low-quality assets (as defined in Regulation W) at the price paid by the bank for the Eligible ARS plus any accrued but unpaid interest and to compensate Bank promptly for any losses incurred upon sale of any Eligible ARS.
- Bank, Wachovia, and WFC must remain "well capitalized" as defined in the OCC's prompt corrective action regulation and the Board's Regulation Y, respectively, until Wachovia purchases the Eligible ARS from the Bank.⁹
- Bank may not rely on this exemption to purchase Eligible ARS from its affiliate until WFC assumes or succeeds to Wachovia's obligations under the Repurchase Agreement, Wachovia's obligation to repurchase any Eligible ARS that become low-quality assets, and Wachovia's obligation to compensate Bank promptly for any losses incurred upon sale of any Eligible ARS.

In light of these considerations, the covered transactions between Bank and its affiliate, Wachovia Securities, appear to be consistent with the

⁹ See 12 CFR 6.4 and 12 CFR 225.2(r), respectively.

purposes of section 23A and in the public interest. Accordingly, the Board hereby grants the requested exemption, subject to the conditions and limits discussed above.

This determination is specifically conditioned on compliance by Wachovia and Bank with all the commitments and representations made to the Board in connection with this exemption request. These commitments and representations are deemed to be conditions imposed in writing by the Board in connection with granting the request and, as such, may be enforced in proceedings under applicable law. This determination is based on the specific facts and circumstances described in your correspondence and this letter. Any material change in those facts or circumstances or any failure by WFC, Wachovia, or Bank to observe any commitments or representations may result in a different conclusion or in a revocation of the exemption.

Very truly yours,

(signed)

Robert deV. Frierson
Deputy Secretary of the Board

cc: David Tatum, Vice President
Federal Reserve Bank of Atlanta
Federal Deposit Insurance Corporation