

Federal Reserve Bank of San Francisco
101 Market Street, San Francisco, California 94105

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To State Member Banks, Bank
Holding Companies, Financial Holding
Companies, Foreign Bank Offices and
Savings and Loan Holding Companies
in the Twelfth Federal Reserve District

SR 11-15 Disposal of Problem Assets Through Exchanges

On December 21, 2011, the Board of Governors of the Federal Reserve System issued SR 11-15 (Disposal of Problem Assets through Exchanges). This letter applies to all state member banks, bank holding companies and their nonbank subsidiaries, and savings and loan holding companies that engage in asset exchange transactions, including those with \$10 billion or less in consolidated assets.

Financial institutions are increasingly exploring strategies to dispose of or reduce nonperforming assets and other real estate owned (OREO). Some of these strategies include so-called “asset exchanges,” whereby third parties or marketing agents have offered to purchase problem assets from institutions and replace them with performing assets. While such transactions, if properly executed with reputable counterparties and subjected to the appropriate level of due diligence, could achieve the objective of reducing nonperforming assets on financial institutions’ balance sheets, Federal Reserve staff have been made aware of transactions that may present significant risk to institutions and could compromise their safety and soundness. To date, these transactions have been encountered primarily at smaller community banks.

The Federal Reserve is issuing the attached guidance, including an example of an asset exchange transaction, to highlight the potential risks associated specifically with transactions which may reduce problem assets in the short term, but where a lack of appropriate, up-front due diligence may result in heightened risks over the longer term. In addition, inappropriate assumptions used in determining the fair value of the purchased assets may result in institutions being required to recognize losses shortly after inception of the transaction.

Please review and disseminate this guidance within your organization as appropriate. If you have any questions regarding this guidance, please contact David Doyle, Senior Manager and Credit Risk Coordinator at the Federal Reserve Bank of San Francisco. Mr. Doyle can be reached at (213) 683-2814.

Additional Information

All circulars and documents are available on the Internet through the Federal Reserve Bank of San Francisco’s website, at <http://www.frbsf.org/banking/letters>.

For additional information, please contact:

Federal Reserve Bank of San Francisco
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(213) 683-2814

Attachment: [Disposal of Problem Assets through Exchanges \(PDF\)](#)

[Asset Exchange Example \(PDF\)](#)