The Meeting of the Systemic Resolution Advisory Committee

of the

Federal Deposit Insurance Corporation

Held in the William Seidman Center

Federal Deposit Insurance Corporation Building

Arlington, Virginia

Open to Public Observation

December 10, 2014 - 9:03 A.M.

The meeting of the FDIC Systemic Resolution Advisory Committee ("Committee") was called to order by Martin J. Gruenberg, Chairman of the Board of Directors, Federal Deposit Insurance Corporation ("Corporation" or "FDIC").

The members of the Committee present at the meeting were: Anat R. Admati, George G.C. Parker Professor of Finance and Economics, Graduate School of Business, Stanford University, Stanford, California; Michael Bradfield, Mercersburg, Pennsylvania; H. Rodgin Cohen, Senior Chairman, Sullivan & Cromwell LLP, New York, New York; William H. Donaldson, Chairman, Donaldson Enterprises, New York, New York; Peter R. Fisher, Senior Managing Director, BlackRock Investment Institute, New York, New York; Janine M. Guillot, Former Chief Operating Investment Officer, CalPERS, Sacramento, California; Richard J. Herring, Co-Director, The Wharton Financial Institutions Center and Professor of Finance, The Wharton School, University of Pennsylvania, Philadelphia, Pennsylvania; Simon Johnson, Ronald A. Kurtz Professor of Entrepreneurship, MIT Sloan School of Management, Cambridge, Massachusetts; Donald L. Kohn, Senior Fellow, Economic Studies Program, Brookings Institution, Washington, D.C.; Douglas L. Peterson, President and Chief Executive Officer, McGraw Hill Financial, New York, New York; John S. Reed, Former Chairman, Corporation of MIT, New York, New York; Paul A. Volcker, Chairman, Trustees of the Group of 30, New York, New York.

Members Michael C. Bodson, President and Chief Executive Officer, The Depository Trust and Clearing Corporation (DTCC), New York, New York; Charles A. Bowsher, Bethesda, Maryland;

Thomas H. Jackson, Distinguished University Professor and President Emeritus, Simon Business School, University of Rochester, Rochester, New York; John A. Koskinen, Former (Non-Executive) Chairman of the Board of Freddie Mac, Washington, D.C.; Gary H. Stern, Chairman of the Board of Directors, National Council on Economic Education, New York, New York; and David J. Wright, Secretary-General, International Organization of Securities Commissions, were absent from the meeting.

Members of the Corporation's Board of Directors present at the meeting were: Martin J. Gruenberg, Chairman; Thomas M. Hoenig, Vice Chairman; Jeremiah O. Norton, Director (Appointive); and Thomas J. Curry, Director (Comptroller of the Currency).

Corporation staff who attended the meeting included: John P. Almand, Steven O. App, Cheryl Bates, Ann M. Battle, Annmarie H. Boyd, Robert L. Burns, Fred Carns, Patricia A. Colohan, Kymberly K. Copa, Carolyn D. Curran, Christine M. Davis, Nancy DelCastillo, Ricardo R. Delfin, Doreen R. Eberley, Bret D. Edwards, Diane Ellis, Joseph Fellerman, Ralph E. Frable, Judy E. Gross, Barbara Hagenbaugh, Herbert J. Held, Michelle A. Heller, Martin D. Henning, Brent D. Hoyer, Mona K. Jabbour, Craig R. Jarvill, Kathy Kalser, Penny B. King, Rose M. Kushmeider, Alan W. Levy, Roberta K. McInerney, Thomas A. Murray, Arthur J. Murton, Richard Osterman, Bimal V. Patel, N. Michelle Rose, Barbara A. Ryan, R. Penfield Starke, Marc Steckel, Travis M. Sumner, Maureen E. Sweeney, F. Angus Tarpley III, David Wall, and Barry C. West.

Paul M. Nash, Senior Deputy Comptroller and Chief of Staff, Office of the Comptroller of the Currency; William A. Rowe, III, Deputy to the Chief of Staff and Liaison to the FDIC, Office of the Comptroller of the Currency; and Jonathan Fink, Assistant Director, Bank Activities and Structure Division, Office of the Comptroller of the Currency, were also present at the meeting.

Chairman Gruenberg opened and presided at the meeting. He began by welcoming the Committee members and noting that the Committee has been extraordinarily helpful to the FDIC on the numerous issues it has confronted in developing the capability to manage an orderly failure of a systemically important financial institution ("SIFI").

Chairman Gruenberg then provided an overview of the meeting agenda, noting that it highlights the substantial progress that has been made over the past year and focuses on several key

areas: (1) the process for the resolution plans or so-called "living wills" that companies must submit under Title I of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"); (2) resolution plan transparency; (3) recent international developments; (4) the new protocol that has been agreed to by the International Swaps and Derivatives Association ("ISDA"); and (5) the orderly liquidation authorities under Title II of the Dodd-Frank Act. He advised that, in August 2014, the FDIC and the Board of Governors of the Federal Reserve System ("Federal Reserve") sent letters to the 11 most significant SIFIs that submitted resolution plans under the Title I requirements; and that staff would update the Committee on the resolution planning process and discuss the explicit directions provided to these 11 firms concerning the steps that need to be taken to improve their resolution plans. He also advised that, as part of the discussion on resolution planning, Member Herring would provide a presentation on the issues related to improving transparency of the resolution plans. With respect to recent developments on international resolution planning issues, particularly cross-border cooperation with the other major jurisdictions throughout the world, he noted that the European community has undertaken significant institution building in the aftermath of the crisis, with European Union ("EU") member countries implementing a single supervisory mechanism and the European Parliament approving the creation of a single resolution mechanism for Europe; that the European Commission ("EC") is actively engaged in establishing that institution and installing its board members and initial staff in the first quarter of 2015; and that Olivier Salles from the EC would participate in the meeting via video conference to discuss the progress that has been made on setting up the new institution and its authorities. Noting that the automatic termination of derivative contracts in the event of an insolvency proceeding was one of the key stabilization issues during the recent crisis, Chairman Gruenberg advised that staff would describe the new protocol that has been agreed to by the ISDA in an effort to address one of the core challenges to maintaining financial stability and an orderly resolution of a SIFI. Finally, he advised that staff would outline the progress that has been made over this past year relating to the FDIC's Title II orderly liquidation authorities, including an approach for winding down a SIFI under a Title II resolution. He noted that the FDIC recently hosted a principal-level exercise recently with the United Kingdom ("U.K."), which was attended by the Chancellor of the Exchequer, the Governor of the Bank of England, and the three Deputy Governors of the Bank of England, as well as the U.S. Secretary of the Treasury, the Chairman of

the Federal Reserve, and the heads of the U.S. bank regulatory agencies to explore issues relating to how the U.S. would cooperate in the event of a failure of a systematic U.S. institution with cross-border operations in the U.K. and, in the alternative, a failure of a U.K. institution with cross-border operations in the U.S. Chairman Gruenberg then introduced Arthur J. Murton, Director of the Office of Complex Financial Institutions ("OCFI") to begin the first panel presentation.

Mr. Murton advised that the first panel would report on the Title I resolution planning process, including the feedback and guidance that the FDIC and the Federal Reserve have jointly provided on the resolution plans, the process of engagement with the firms on their plans, and the potential for improving transparency of the plans. He then introduced the panel members: Herbert J. Held, Associate Director, OCFI; David N. Wall, Assistant General Counsel, Complex Financial Institutions Section, Legal Division; Robert L. Burns, Deputy Director, Complex Financial Institutions, Division of Risk Management Supervision ("RMS"); and Richard J. Herring, Co-Director, The Wharton Financial Institutions Center and Professor of Finance, The Wharton School, University of Pennsylvania (also a Committee member).

Mr. Held began the presentation by noting that, in August 2014, the first 11 firms that filed Title I resolution plans received very specific feedback on their plans, as well as general feedback on issues to be addressed in the plans. He advised that the FDIC and the Federal Reserve jointly identified serious shortcomings to the plans and instructed the firms to correct these problems in their 2015 plans; that one major shortcoming was the reliance on unrealistic or inadequately supported assumptions, such as the likely behavior of customers, counterparties, investors, and central clearing facilities; and that another major shortcoming was the failure to identify changes to their structure and practices to enhance the likelihood of an orderly resolution. He also advised that the FDIC determined that each of the plans would not facilitate an orderly resolution under the U.S. Bankruptcy Code; that the FDIC and Federal Reserve determined that the firms must take immediate actions to improve their resolvability through improvements in their 2015 resolution plans; and that, in the event the firms have not changed their plans for their July 2015 submissions and responded to the identified shortcomings, the FDIC and the Federal Reserve expect to use the authority under section 165(d) of the Dodd-Frank Act to determine that a resolution plan does not meet the requirements of the Dodd-Frank

Act. He briefly outlined some of the changes that are expected with respect to the firms' resolution plans to demonstrate they are making significant progress to improve resolvability under bankruptcy, including: (1) establishing a rational, less complex legal structure that provides a better alignment of the legal entities and business lines to facilitate a restructuring or downsizing; (2) developing a clean holding company structure—with only equity, debt, and investments in subsidiaries at the parent level—that supports resolvability and avoids the entanglements of cross-guarantees and other investments at the holding company level; (3) amending financial contracts with early termination rights to conform to the industry-wide ISDA contract protocol; (4) ensuring continuity of shared services that support critical operations and core business lines throughout the resolution process; (5) demonstrating operational capabilities and resolution preparedness; and (6) increasing transparency of the resolution plans. He concluded by noting that the FDIC and the Federal Reserve responded to Wells Fargo & Company's resolution plan in November 2014, determining that it provided a basis for a resolution strategy under bankruptcy which, if fully developed in the future, could reduce the risk that the firm's failure would pose to the stability of the U.S.; and that the firm's 2015 plan would need to demonstrate significant progress in addressing the identified shortcomings.

Next, Mr. Burns briefly discussed the interactions of the FDIC and the Federal Reserve with the firms in an effort to dramatically improve their engagement with the firms throughout the Title I planning process. He noted that, beginning in September 2014, the FDIC and the Federal Reserve have held a series of meetings with each of the firms to discuss the shortcomings identified in their resolution plans and to respond to questions regarding the changes they have been directed to make in their existing organizational structures and practices to improve their resolvability; that the FDIC and the Federal Reserve are planning to hold additional meetings with the firms in early 2015 to discuss how they intend to address some of the major issues in their 2015 plan submissions; and that the FDIC and the Federal Reserve have also increased their engagement through ongoing dialog with the firms during the plan review process, as well as meetings with onsite staff of the FDIC and the Federal Reserve. He also noted that engagement with the firms has increased in the supervisory area with new supervisory activities related to recovery and resolution; that the Federal Reserve, with participation from FDIC supervisory staff, conducted a targeted and horizontally executed supervisory assessment of the firms' recovery and resolution preparedness to

identify and minimize risks to recovery and resolution; and that these supervisory activities are focused on assessing: (1) the firms' progress in addressing the shortcomings identified in the supervisory letters sent to the firms, and (2) assessing the progress the firms are making in meeting the supervisory expectations established by the Federal Reserve's SR Letter 14-1 issued in January 2014, which outlines minimum capabilities that certain large bank holding companies should maintain for effective recovery and resolution preparedness. He concluded by emphasizing that the supervisory activities are intended to complement, but not replace, the annual resolution plan review process.

During the discussion that followed, Committee members raised a number of issues relating to the Title I resolution planning process. Member Johnson began by asking whether the firms have been asked to consider how bankruptcy procedures would be handled by judges in the U.K. or other jurisdictions, and whether Title I was feasible and attainable in the absence of a treaty between the U.K. and the U.S. to cooperate on a bankruptcy resolution. In response, Mr. Murton noted that global cooperation on a resolution involving a bankruptcy has presented a challenging problem; that the firms have been asked to explain how their entry into the bankruptcy process would work, both in the U.S. and abroad; and that, if their plan assumes cooperation from foreign jurisdictions, the firms must explain the basis for that cooperation from other bankruptcy authorities. Member Fisher asked whether it was realistic to expect firms to change their corporate structures within a short timeframe, particularly if they must obtain approval from regulatory agencies in other jurisdictions, and to what extent the capital structure of holding companies can be simplified. Mr. Held responded by advising that the firms would be required to make changes to their corporate structures, as well as their back office systems; that many of the firms have multiyear plans for changes to their systems; that the firms should have a plan with timetables, budgets, and goals when they file their 2015 resolution plans; and that the firms' capital structures would be better if the holding company does little business other than investing in its operating subsidiaries, both in terms of debt and equity. Member Fisher also suggested that the firms are being asked to have a plan for a bankruptcy plan in the future; and that, in reality, the firms are being asked to have a strategic plan to reorganize so that they have a bankruptcy plan. Mr. Murton responded by noting that the firms have been told that they need to demonstrate significant progress toward improving their resolvability in their 2015 resolution plans;

that their plans should indicate what changes would be made and how long it would take to make those changes; and that the amount of time necessary will depend on the changes that need to be made. Chairman Gruenberg emphasized that the FDIC and the Federal Reserve should have a better estimate of the timeframe that will be required after the submission of the next round of resolution plans in July 2015; that the agencies will be looking for tangible steps to be taken by the firms to address some of the issues in their next plan submissions; and that the firms must lay out a work plan for addressing all of the issues with a timeframe and budget.

Member Donaldson asked what the timetable would be on the next step after the 2015 resolution plans have been submitted. In response, Mr. Murton advised that, after the plans are submitted in July 2015, they would be evaluated by the FDIC and the Federal Reserve; that, if the agencies make a determination that the plans do not meet the standard set forth in the Dodd-Frank Act, then the applicable statutory provisions require the FDIC and the Federal Reserve to issue a notice of deficiencies to the firms, to which they must respond within 90 days; that, in the event the response was determined to be insufficient, the statute permits further sanctions, such as higher capital liquidity or restrictions on operations or activities; and that, if those measures do not correct the situation, the statute also provides that, after a two-year period, the FDIC and the Federal Reserve Board could require further steps, such as divestiture.

Director Curry complimented the staff for their work on the resolution plans, emphasizing that the simplification of the firms' corporate structures should not focus solely on the number of legal entities because it also was a risk management problem for the entire organization when a disconnect exists between the legal entities and the overall lines-of-business approach that has been prevalent. Noting that the onsite supervisory work represents an improvement, Director Curry asked whether existing resources or regimes were being leveraged in terms of recovery planning. In response, Mr. Burns advised that the onsite supervisory work was an effort being led by the Federal Reserve with the participation of FDIC supervisory staff; that, during the initial phase, a considerable amount of time has been spent inventorying all of the available information resources that could be leveraged, including the firms' self-assessments against the expectations laid out in the Federal Reserve's SR Letter 14-1, information obtained through the resolution planning process and prior plan reviews, and supervisory findings of other regulatory agencies; and that the

next phase would involve outreach to the firms for additional information. Emphasizing that each firm's plan should be individually evaluated because some firms may be closer to resolvability under bankruptcy than other firms, Director Norton cautioned that evaluating the resolution plans as a group and signaling that every firm is on the same timeline could create a disincentive for actual change.

Member Admati expressed concern regarding the assumptions that the firms are expected to make for a scenario that leads to resolvability, noting that there is a continuum of scenarios and the firms may not have enough information to develop a plan that takes into account all of the different scenarios. In response, Mr. Murton agreed that there are innumerable scenarios that the firms could face; that the firms have been asked to consider a severely-adverse economic scenario and assume the firm would be facing bankruptcy without access to the market for funding and capital; and that going forward the firms may be required to expand the set of scenarios for purposes of the Title I process. With respect to ensuring international cooperation on a resolution, Member Cohen suggested that, a simple "three-page" treaty would create highly-desirable certainty; and that efforts to make the holding companies' structures cleaner would benefit from the issuance of final rules on Total Loss Absorbing Capacity ("TLAC")—debt and equity available to absorb losses in a resolution—which is a key ingredient for resolvability. Mr. Murton agreed that the firms' long-term debt, both issued externally at the parent and in the key material legal entities, was a very important aspect of resolvability; and that the agencies recognize that the interplay between the issuance of TLAC regulations and the timing of the resolution plans. Chairman Gruenberg noted that the afternoon session would include a discussion of the TLAC agreement and the forthcoming rules. Noting that the rest of the world appears to be moving toward Title II resolvability, Member Kohn asked whether there was a potential conflict between organizing a holding company for a universal bank in Europe for resolution versus the way the FDIC would want them organized for bankruptcy in the U.S. In response, Mr. Murton indicated that all of the steps the firms are being directed to take under the Title I process also would facilitate the Title II process and make that result less likely. Vice Chairman Hoenig asked whether there would also be a treaty focused around Title II if there was one focused around Title I, since the first issue to decide would be which rule of law the firms would be subject to. Member Cohen agreed that any treaty would initially need to deal with the issue of which rule of law works best, noting that the FDIC's own studies indicated

that a U.S.-U.K. treaty would address approximately 90 percent of the issue.

Next, Member Herring presented some of the highlights from recent research on improving the transparency of the resolution plans. He began by noting that the core problem was the huge number of opaque interconnections among these firms with hundreds or thousands of subsidiaries that, in the recent crisis, impeded effective oversight before the crisis broke out and greatly complicated crisis management and resolution ex-post. He also noted that these firms function globally as integrated units, but need to be taken through a resolution process as separate legal entities; that the huge number of separate legal entities makes it enormously difficult to coordinate resolutions in multiple jurisdictions, inevitably resulting in the loss of any going concern value; and that the current disclosures arguably are insufficient for creditors, counterparties, or other interested parties to evaluate the situation. He briefly discussed some of the dimensions of complexity in these firms, noting that their interconnections, the extent of their cross-jurisdictional activities, and the large number of subsidiaries with both financial and nonfinancial activities have increased their organizational complexity. He suggested that regulation often increases the corporate complexity in these firms; that the largest banks have approximately two and one-half times as many subsidiaries as nonfinancial corporations of comparable market capital and size; that regulatory requirements in the U.S. have emphasized subsidiarization and corporate separateness from the very beginning of the Federal Reserve System; and that regulators have the opportunity to improve transparency, for example, by improving disclosure requirements for the public section of the resolution plans. He indicated that tax incentives also have contributed to the increase in corporate complexity of these firms; that a large proportion of the firms' subsidiaries are located in off-shore tax havens and structured solely for the purpose of minimizing taxes; and that the potential costs and other implications of dealing with the resulting complexity create an obstacle to an orderly resolution of these firms that has not been taken into account in tax policies. Finally, he suggested that current disclosure practices have actually hindered public monitoring of the firms' progress toward simplification; that it was important for the public to be able to monitor progress across institutions, as well as for the same institution over time; and that the disclosures in the resolution plans are inadequate because the definitions and terminology are not applied uniformly by the firms, resulting in

inconsistent disclosure of information. Mr. Herring then outlined several recommendations to improve transparency in the resolution plans, including that: the definition of material entity should be standardized based on consolidating statements that take into account operating entities above a certain threshold and intermediate-level holding companies that issue public debt; the plans should be accompanied by an organizational chart showing the hierarchy of material entities; information on material entities should include data relevant to creditors, counterparties, and regulatory authorities; entities not considered material should be grouped into standardized categories, with each group identified by name, location, and primary function; information on foreign branches should be disclosed; and consideration should be given to disclosures relating to nonconsolidated variable interest entities. He concluded by suggesting that disclosures of relevant data in the firms' annual reports, Securities and Exchange Commission ("SEC") filings, and other supervisory reports should be reviewed and reconciled; that global systemically important banks ("G-SIBs") should be held to a higher standard with regard to disclosure; and that the Financial Stability Board ("FSB"), which has responsibility for designating G-SIBs, should take the lead in harmonizing data definitions and disclosure practices to improve transparency for this very complex category of institutions.

In the discussion that followed, Committee members offered their comments on a number of issues regarding improving transparency in the resolution plans. Member Johnson emphasized that it was important to consider the limitations in the existing data when comparing U.S. banks with international banks to ensure an "apples-to-apples" comparison. In response, Member Herring agreed, noting that there are instances involving data on subsidiaries where he encountered substantial differences between reporting under International Financial Reporting Standards ("IFRS") and Generally Accepted Accounting Principles ("GAAP"). Member Fisher observed that the materiality issue was a key aspect of motivating boards of directors and management to make the difficult decisions necessary to comply with Title I. On the issue of the root causes for the complexity in these firms, Member Guillot expressed concerns regarding the unintended consequences of pushing for simplification of corporate structures through the resolution planning process without addressing the underlying drivers of, and reasons for, that complexity.

Observing that Member Herring's research has ramifications

beyond the resolution plans, Member Cohen suggested that one of the root causes of the financial crisis in 2008 and the contagion that ensued was the absence of transparency; that investors and creditors could not figure out what every institution had; and that, while progress has been made in many ways with respect to creating more resilient banks, little work has been done to even broach the disclosure and transparency issue. Noting that there has been more disclosure from banks, he stressed that the industry was literally operating under guidelines from the SEC on disclosure which date back to the 1970s; and that the bank regulatory agencies and the SEC should initiate efforts to enhance that disclosure. Member Bradfield asked whether the Office of Financial Research ("OFR") has the authority to request this data. Member Herring responded by suggesting that the most effective mechanism would be to collect this data in the Title I process by working through the FSB to make it part of the overall criteria, particularly since the OFR may not have the authority to request it. With respect to the issue of taxes as a root cause of corporate complexity, Member Kohn indicated that simplifying the number of entities could raise taxes for U.S. institutions, placing them at a disadvantage relative to their international peers. Member Admati concluded the discussion by noting that the key constituency of the information disclosures is the investors, especially the equity investors.

Chairman Gruenberg then announced that the meeting would briefly recess. Accordingly, at 10:39 a.m., the meeting stood in recess.

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The meeting reconvened at 10:49 a.m. that same day, at which time Mr. Murton introduced Oliver Salles, Head of the Task Force for the Establishment of the Single Resolution Board in the EC's Directorate-General for Financial Stability, Financial Services, and Capital Markets Union, and Sven Gentner, a representative from the European Union ("EU") delegation in Washington, D.C., who both joined the meeting via video conference to discuss the progress the EU is making with respect to resolution processes and establishment of the Single Resolution Board ("SRB").

Mr. Salles began by advising that the EU has taken some important steps over the last several years as it coordinated reactions to the financial crisis; that the new SRB would be one of two key elements of the Banking Union, with one being the

Single Supervisory Mechanism ("SSM") and the other being the Single Resolution Mechanism ("SRM"); and that the scope of the SRM would cover the same participating member states and financial institutions directly covered by the European Central Bank ("ECB") under the SSM. He briefly outlined the role and powers of the SRB, noting that this new mechanism would provide the EU with a more coordinated resolution system; that it would facilitate more centralized decision making for responding to potential resolution cases; and that it would have a financing capacity through the Single Resolution Fund ("SRF"), which would be funded with contributions from supervised financial institutions. With respect to the SRB's role, he advised that the SRB would have the task of coordinating the effective functioning of the SRM; that the SRB would be directly in charge of all significant entities supervised by the ECB and monitor all cross-border groups established in the Eurozone; and that national resolution authorities would be responsible for all other types of institutions, except when the SRB decides or was asked to take over direct responsibility on specific resolution cases.

Mr. Salles briefly highlighted a number of dates and milestones relating to the establishment of the SRB, noting that the SRM regulation became effective in August 2014; that the EC was asked to take responsibility for the establishment and initial operation of the SRB; that he was appointed as Interim Chair of the SRB in September 2014 and would serve until it reached full capacity; that the SRB would become operational in January 2015; that a permanent board for the SRB was expected to be appointed and take office during the first quarter 2015; and that the SRB would continue the process of recruiting staff, with the expectation that the SRB would reach a total staff of approximately 250 positions by the end of 2016-2017. He emphasized that 2015 would be primarily a phase of preparation, with the SRB starting its recovery and resolution planning activities; and that, beginning in January 2016, the SRB would have the full powers and capacity to address resolution cases, propose resolution schemes, and use the Resolution Fund. He noted that a significant portion of the powers and coordination capacity would be the responsibility of the SRB, and that a portion of the actions would continue to be taken at the national level by the national resolution authorities to create a solid and cooperative dynamic between the EU level and the national level. He described several of the working groups that have been established to: build a cooperation framework between the SRB and the national resolution authorities; secure the exchange information with the ECB, national resolution

authorities, and other supervisory authorities to ensure access to necessary supervisory data; and establish the initial priorities and work program of the SRB in coordination with the national resolution authorities.

In conclusion, Mr. Salles emphasized that, following completion of the initial preparatory and coordination phase in early 2015, the SRB should be fully established and in a position to start coordinating the drafting of resolution plans for the most important institutions in Europe; and that the SRB and the SRM as a whole could be ready to face potential resolution cases in early 2016.

After thanking Mr. Salles for the presentation, Chairman Gruenberg began the discussion that followed by asking if the SRB was establishing a close working relationship with the SSM to ensure coordination between the supervisory authorities and resolution authorities, which would be critical for an effective resolution process. In response, Mr. Salles indicated that the SRB was working closely with the SSM and the ECB, which are both of critical importance; that the ECB would be one dimension of this cooperation because it would trigger the resolution process; and that another important dimension of cooperation would be the exchange of information and data, which most likely would be established through a formal memorandum of understanding between the SSM and the SRM. Noting the complexities and different levels of the EU decision making process, Member Johnson asked what the overall objectives of the SRB were with respect to the balance between the national resolution authorities and the SRB. Mr. Salles responded by advising that the overall objective of establishing the SRB was to contribute to financial stability in Europe; that resolution cases would be managed in a more coordinated and planned way to avoid the bad experiences over the last three or four years involving the use of taxpayers' money to save financial institutions; that it would be the responsibility of the ECB and the SRB to monitor and oversee the resolution planning for the 120 most important institutions in Europe; and that the SRB would be responsible for the coordination of the resolution planning and potential resolution cases for cross-border groups. He emphasized that the resolution decisions in Europe would be guided and coordinated by the SRB, but the actual implementation of potential resolution cases would be handled by the national resolution authorities under the coordination of the SRB.

Member Admati asked how an interaction between the SRB and the resolution authorities would operate. In response, Mr.

Salle noted that the SRB was still in the startup phase and that many aspects of the EU resolution mechanism need to be clarified, including the detailed structure of resolution plans; that it was uncertain when the national resolution authorities would be established in the member states because of the diverse spectrum of situations among the participating member states, with some important member states, such as Germany, Netherlands, and France having well-established resolution authorities, while some of the smaller member states are expected to rely on the SRB to assist in establishing their resolution authorities; and that the national resolution authorities would be members of the plenary session of the SRB, which should facilitate cooperation among the national resolution authorities to make decisions and prepare the necessary instruments for resolution cases. Member Peterson asked how the SRF would be established and how the network of deposit insurance schemes would operate at the national level. In response, Mr. Salles indicated that the SRF would be established with contributions from the member states over an eight-year period; and that the contributions to the SRF in the early years would be coordinated at the national level, with the SRF becoming mutualized over eight years to establish an EU-based SRF. Mr. Gentner clarified the difference between the SRF and the Deposit Guarantee Funds in the EU, advising that these are two separate funds; and that the SRF would start with national compartments before becoming a completely EU-based SRF, while the Deposit Guarantee Funds would remain national funds guided by EU rules. In response to a question from Member Cohen regarding whether the SRF was a liquidity-type fund lending only against collateral or a loss absorbency fund covering shortfalls, Mr. Gentner advised that the SRF would be a fund that could absorb losses.

With respect to the EU resolution process, Member Bradfield asked whether the goal would be liquidation or restructuring. Noting that both options would be possible with the resolution tools provided under the EU Bank Recovery and Resolution Directive, Mr. Salles advised that there has not been a final decision on whether the end result should be liquidation or restructuring, and that the SRB's experience over the next 12 to 24 months should provide more insight and clarity on some of the options. Member Peterson asked when the largest EU banks would have to submit their initial resolution plans and whether the SRB would have specific authority to mandate changes to the plans. In response, Mr. Salles noted that the SRB would be addressing the resolution plans as one of its first priorities over the next several months, focusing on two different elements: (1) the capacity of the SRB to coordinate and monitor

resolution plans and (2) the state of participation and readiness in some of the larger member states regarding important institutions; and that an ambitious objective would be to have partial resolution plans for some of the largest institutions by the end of 2015. Noting that remarkable progress has been made in the EU jurisdictions with respect to resolution authorities, Member Volcker expressed concern regarding whether the EU's resolution mechanism would mesh well with a Title I resolution. Chairman Gruenberg responded by emphasizing that the FDIC has placed a high priority on its cross-border relationship with the EU's new SRM, which would fill a critical gap in the international framework to effectively address cross-border issues. Mr. Salles added that a substantial amount of work still needs to be done on the EU's resolution mechanism; and that it would take time to correctly establish the SRB and coordination between the EU and the national level.

Chairman Gruenberg announced that the meeting would recess for lunch. Accordingly, at 11:48 a.m., the meeting stood in recess.

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The meeting reconvened at 1:22 p.m. that same day, whereupon Chairman Gruenberg thanked Member Herring for his insightful presentation in the earlier session, noting that he has provided a template from which the agencies can work as they engage the firms relating to the transparency of their resolution plans. He then requested that Mr. Murton introduce the next panel to begin the afternoon session of the meeting.

Mr. Murton observed that one of the impediments to resolution under bankruptcy identified in the resolution planning process was the ability to terminate over-the-counter ("OTC") derivatives in a resolution. He then introduced Ann Battle, Counsel, Complex Financial Institutions Section, Legal Division, advising that she would provide an update on the new ISDA resolution stay protocol.

Ms. Battle began the presentation with some background on the issue of the ability of parties in OTC derivatives to exercise termination rights and other remedies, such as setoff against collateral, if their counterparty or any affiliate is subject to resolution or insolvency proceedings. She advised that, if not exercised in an orderly manner, these termination rights and other remedies could result in additional defaults,

for example, affiliate defaults, unhedged positions, fire sales of collateral, and a number of other negative consequences to financial stability; that Title II of the Dodd-Frank Act and the Federal Deposit Insurance Act (the "FDI Act") both contain a one-business-day stay before a financial company's counterparties may exercise these termination rights and other remedies; and that, during the stay period, the FDIC as receiver may transfer the contracts or take certain other actions, which, if successful, result in the counterparties no longer having the right to terminate or exercise other remedies as a result of the resolution proceedings. Noting that the FDIC as receiver also would have this stay authority under the Dodd-Frank Act for financial companies resolved under Title II, she advised that the stay may not always be enforceable in a cross-border context; and that the U.S. Bankruptcy Code does not stay the exercise of early termination rights and other remedies. She continued, advising that the ISDA—which is the trade association for buy-side and sell-side participants in the OTC derivatives market and published most of the standard documentation used for OTC derivatives worldwide with certain exceptions—formed a working group in early 2013 to consider these issues; that, in November 2013, the FDIC, Bank of England, BaFin, and FINMA wrote a joint letter to ISDA requesting that the standard documentation be amended to provide for a short-term suspension of early termination rights and other remedies on the basis of a commencement of the insolvency or resolution proceeding or the exercise of resolution power with respect to a counterparty or its specified entity, guarantor, or credit-support provider; that the Japan FSA and France subsequently joined in the recommendation made by the other authorities; and that, in November 2014, ISDA issued the Resolution Stay Protocol.

Ms. Battle briefly described the two primary sections of the ISDA Resolution Stay Protocol. She explained that Section 1 provides a mechanism for the enforcement of the one-business-day limited stay provisions under Title II of the Dodd-Frank Act and the FDI Act to foreign counterparties of the insured depository institutions ("IDIs") that are being resolved under the FDI Act and of financial companies for which the FDIC has been appointed receiver; that this section provides for cross-border application of the temporary stay; that the adhering parties "opt-in" to the stay provisions in the special resolution regimes that may apply to their OTC derivatives counterparties that are also adhering parties; that the special resolution regimes initially include Title II and the FDI Act, as well resolution regimes with temporary stays on close-out rights in the U.K., Germany, Switzerland, Japan, and France; and that

resolution regimes adopted in other FSB jurisdictions that include certain creditor protection provisions may also qualify as special resolution regimes under Section 1. After describing the opt-in provisions in further detail, she explained that Section 2 addresses one of the impediments to orderly resolution under the U.S. Bankruptcy Code by providing for temporary stays of termination rights for cross-defaults resulting from affiliate insolvency proceedings under a limited number of U.S. resolution regimes, including the U.S. Bankruptcy Code and the FDI Act; that, upon commencement of the proceedings, adhering parties agree to be stayed for the longer of one business day and 48 hours, provided that certain creditor protection provisions continue to be satisfied; and that, similar to under the statutory resolution regimes, the temporary stay becomes permanent if certain debtor and possession requirements or transfer requirements are satisfied.

Finally, Ms. Battle provided a brief overview of adherence to the ISDA Resolution Stay Protocol and related regulation, advising that the top 14 G-SIBs, three G-SIBs outside of the U.S., and one additional firm outside of the U.S. adhered to the protocol in November 2014; that Section 1 would take effect on January 1, 2015, with respect to these initial adhering parties; and that Section 2 would not take effect until the effective date of regulation requiring G-SIBs and potentially certain other financial entities to amend their OTC derivatives contracts in a manner consistent with the protocol. Upon related regulation becoming effective, she indicated that all counterparties of regulated entities, including buy-side market participants and smaller dealers, would have to adhere to the ISDA Resolution Stay Protocol or enter into substantially similar contractual amendments to their OTC derivatives contracts; that, with respect to subsequently adhering parties, Section 1 and Section 2 would take effect simultaneously on the effective date of regulation requiring the amendments to OTC derivatives contracts; and that implementation of the protocol would likely require regulatory activity in the U.S.

In the brief discussion that followed, Committee members asked for and received clarification on how the claims and rights of parties to OTC derivatives would be handled under the ISDA Resolution Stay Protocol, such as a hypothetical situation involving a potential transfer between an adhering party and a non-adhering party. Member Bradfield inquired whether there was any mechanism that, despite the applicability of the stay, would prevent the holder of the contractual rights from selling the collateral or the counterparty refusing to turn over the benefit

to which the other party to the transaction was entitled, forcing the bankruptcy estate to incur substantial litigation costs in an effort to recover assets. In response, Mr. Wall emphasized that it may not be possible to entirely eliminate the need for judicial enforcement of contractual or legal requirements if parties fail to cooperate, noting that the existence of the ISDA Resolution Stay Protocol should make judicial enforcement more certain and expeditious. In response to Member Bradfield suggesting that some form of penalty may be appropriate to avoid that course of action and prevent systemic issues, Ms. Battle noted that the ISDA Resolution Stay Protocol, especially the contractual opt-in provisions of Section 1 that make the enforcement of the stay against foreign counterparties more certain, would potentially expedite any litigation by establishing a clear contractual agreement that one counterparty breached. In response to a question by Ms. Admati regarding an update on the issue of collateral grabbing, Ms. Battle indicated that OTC derivatives do not encompass the whole universe of qualified financial contracts or financial contracts under the U.S. Bankruptcy Code, noting that there has been some discussion of extending similar provisions like those in the ISDA Resolution Stay Protocol to other qualified financial contracts. Chairman Gruenberg concluded the discussion by emphasizing that there was substantial value in having the ISDA Resolution Stay Protocol as a supplement to the FDIC's statutory authority under the FDI Act and Dodd-Frank to impose a temporary stay; and that substantial progress was being made on this important issue.

Mr. Murton then introduced F. Angus Tarpley, III, Associate Director, OCFI, for a discussion of loss absorbing capacity and the FSB's recent TLAC proposal. Mr. Tarpley began by noting that firms need a sufficient amount of unsecured liabilities to be able to absorb losses, stabilize the critical functions within the organization, and execute a resolution; and that firms also need to hold sufficient equity capital to maximize the chances of a recovery. He advised that, in the U.S., the Federal Reserve has discussed a potential requirement that firms issue minimum amounts of unsecured long-term debt to address the need for loss absorbing capacity; that, internationally, the FSB developed and released for comment a proposal on TLAC that would require a minimum amount of externally-issued TLAC; and that the Basel Committee and the FSB are conducting a quantitative impact study and market survey on a number of issues relating to calibration of amounts, ability of the market to absorb the level of debt required, gaps in coverage, and implementation of the standard at the national level, including in the U.S. He briefly discussed the two key requirements to the TLAC standard,

noting that one was a minimum external TLAC requirement ranging from 16 to 20 percent of risk-weighted assets or twice the Basel III Tier 1 leverage ratio requirement; that the requirement would be applicable to each resolution entity within the group; that there would be a debt component requirement that at least 33 percent of the TLAC requirement be met with either Tier 1 or Tier 2 debt or nonregulatory capital instruments.

In response to Member Admati questioning the emphasis on the need for debt rather than equity, Mr. Murton explained that the FDIC is in favor of having substantial equity in the firm which would reduce the probability of failure, but that there was a need to have something available to absorb losses in a resolution. Mr. Murton and Mr. Tarpley also clarified that TLAC can be equity and debt; that there would be a total TLAC requirement; and that a portion of that requirement would need to be met with either Tier 1 or Tier 2 debt or nonregulatory capital instruments. In response to Member Johnson suggesting that the point of the TLAC requirement was to add some long-term unsecured debt that could be converted to equity under the SPOE strategy more easily with less systemic damage, Mr. Murton agreed, noting that the concept was that these firms issue this debt into the market and buyers of that debt would know that they would be absorbing the losses in a resolution; that there are discussions about whether other financial firms would be able to hold this debt without fear of contagion; and that the private sector buyers of this debt would take the losses, which avoids having the taxpayers bear the losses. Noting that more equity could reduce the probability of default, Chairman Gruenberg stated that experience has shown that the risk of failure exists regardless of the equity level and, when failure occurs, the equity is gone; that the experience in the recent crisis was that the taxpayers stepped into the breach to absorb losses and avoid the consequences of failure; and that the TLAC proposal was an effort to supplement a substantial equity requirement with a debt requirement, which would be available for conversion to equity in the resolution process in order to manage an orderly failure of the firm, supported by private sector creditors rather than taxpayers. Noting agreement with Chairman Gruenberg's comments, Member Johnson suggested that knowing who was holding the debt would be important to facilitate a resolution. In response, Chairman Gruenberg agreed, noting that this debt would be known to the market as being at risk in the event of failure; that investors should understand that they are taking risk by buying this debt, even if the debt is held by a systemically-important financial institution; and that there may be some value in terms of market

signaling and pricing of this debt to reflect the condition of the firm. Member Reed suggested that lenders, when calculating the creditworthiness of the borrower, would look at both their equity and the loss-absorbing capability; that the lender would understand that, if you lend to a firm and it fails, any liabilities of the firm are at risk of loss; and that it would be unlikely that this debt buffer would be available to facilitate a resolution after the equity has been wiped out.

Following additional comments from Committee members on the issue of debt serving as a mechanism to absorb losses in a resolution, Mr. Murton introduced Rose M. Kushmeider, Director of Policy, OCFI, advising that she would provide a brief overview of comments received on the FDIC's Notice on the single-point-of-entry ("SPOE") strategy issued in December 2013.

Ms. Kushmeider began by advising that 29 written comments were received on the SPOE Notice, with the majority of the comments focusing on specific issues, including global cooperation, liquidity and capital, the valuation and claims process, the exit process from the bridge financial holding company, and subsidiarization. With respect to global cooperation, she reported that a number of the comments were generally favorable to the FDIC's efforts in this area but expressed doubt that there would be cooperation in an actual crisis; that a number of comments favored binding agreements with the FDIC to recognize foreign resolution regimes and prevent ring-fencing; that other comments expressed concern regarding change-in-control issues and foreign regulators; and that some comments suggested amending the U.S. Bankruptcy Code to add recognition of foreign resolution regimes. In the area of capital and liquidity, she advised that some comments expressed concern regarding the amount of intercompany debt needed at each subsidiary; that some comments raised concerns on dealing with insolvent subsidiaries, especially if there was insufficient debt at the holding company to absorb those losses; and that other comments questioned the availability of private sector financing in a resolution of a SIFI. On the issue of valuation and claims, she noted that approximately one-half the comments expressed the need for specific information on the valuation and claims process or a valuation model; that some comments highlighted the difficulty of preparing financial statements and disclosure throughout the resolution process; that some comments suggested that there should be the equivalent of a creditors' committee; and that a number of comments emphasized the need to preserve the franchise value of the firm. Turning to the issue of exit from the bridge financial holding

company, she reported that some comments suggested that the FDIC should maximize value from the resolution without regard to the post-resolution structure of the company; that several comments emphasized that the focus should be on maximizing value for the creditors of the company; and that other comments suggested that the goal should be creating multiple firms that are less complex and interconnected. Finally, with respect to subsidiarization and whether companies should have operations abroad in subsidiaries rather than branches to facilitate the resolution process, she advised that a number of comments supported subsidiarization as an effective model; and that other comments indicated that subsidiarization would impede capital and liquidity flows.

Next, Mr. Held presented a brief summary of the plan for winding-down a covered financial company. He began by advising that, in the Title II resolution, the immediate goal would be to stabilize the company, maintain essential services, and describe the plan and actions taken by the FDIC to wind down the covered financial company; that the FDIC has established winding-down as an integral part of the SPOE resolution process; that, in addition to the changes that occur during the bridge period, the FDIC would require the emerging company to agree to continue the winding-down process in post-bridge status; and that the plan would ensure that any emerging entities would not pose a systemic risk and would be resolvable under the U.S. Bankruptcy Code. He continued, advising that the current efforts to simplify operations and provide optionality in resolution would facilitate winding-down under bankruptcy or Title II; that, in Title II, an initial operating agreement would require the new bridge management to formulate a plan to identify and address the causes of the failure to ensure viability, as well as the steps to make the firm smaller and less complex, such as more closely aligning the operations, dividing the company into several companies, or selling parts of entities; and that some parts of the business would likely be liquidated as a result of the failure, even if the entities themselves do not go through an insolvency process. He presented a stylized organization chart illustrating the major entities within the large firm, noting that it would be unlikely that the commercial broker-dealer or wholesale broker-dealer entities would remain unchanged after going through a bridge period of six or nine months because it would be very difficult to retain talent and keep counterparties from moving their business to other institutions.

In the brief discussion that followed, Member Johnson asked

if the FDIC could keep the broker-dealer businesses operating with the same employees and contracts. In response, Mr. Held explained that the companies would stay in business and honor their contracts; that it may be difficult to attract new business to companies in bridge status; that employees may decide not to remain with the companies; and that these types of firms could be wound down in size very quickly by fulfilling contracts or allowing repurchase agreements to mature. Director Norton questioned whether customers may be less likely to move their business elsewhere in a resolution scenario where an operating subsidiary remained open with the Orderly Liquidation Fund ("OLA") as its funding mechanism; and that employees with legal agreements may remain if the operating subsidiary's status has not changed. Member Peterson responded by noting that the OLA funding mechanism may not be enough; that whether or not customers remain may depend on the cause of the crisis and the extent to which the reputation of the business may be damaged; and that access to funding was essential to quickly taking the actions necessary to preserve value and customers. Chairman Gruenberg noted that the expectation under a Title II scenario would be an orderly liquidation of the broker-dealers and wholesale broker-dealers, and the sale of other subsidiaries that retain some market value; that there would be a likely shrinkage of the insured depository itself; and that, if there was any surviving entity, it would be a dramatically smaller and narrower entity, without the systemic ramifications of the entity that entered the process.

Noting that a substantial amount of work has been done with the firms on the Title I resolution plans, Member Peterson asked when the agencies would potentially shift from the position of receiving information from the firms and providing guidance to mandating changes. Chairman Gruenberg responded by advising that the letters that were recently sent to the firms were not advisory; that those letters directed the firms to make specific changes that would result in both structural and operational alterations in the firms; and that the letters sent to the firms represent a threshold step in the whole process, with the FDIC utilizing the resolution plans as a tool to get real-time changes in the structure and operations of these firms that would meaningfully facilitate an orderly failure under the U.S. Bankruptcy Code and, if necessary, under the Title II authority.

In bringing the meeting to a close, Chairman Gruenberg noted that the progress made on the resolution planning process and the directions given to the firms for their compliance over the course of the next few months, together with the development

of the ISDA Resolution Stay Protocol, the movement toward a holding company debt requirement in the U.S. pursuant to the TLAC Agreement, and the progress made on establishing cross-border relationships with key foreign jurisdictions, particularly the United Kingdom, and assisting the EC in the standup of the SRB, have laid the foundation and infrastructure for managing an orderly failure of a SIFI that did not exist five years ago. He observed that each one of these issues was remarkably complex and challenging; that the progress made on the range of the issues that need to be addressed has been substantial, and, taken together, was rather impressive; and that there has been tangible movement toward the capability to manage an orderly failure of one of these firms where the firm suffers the consequences of failure without putting the financial system itself at risk. He concluded by thanking the Committee members for their participation, emphasizing that the Committee's robust discussions and differing viewpoints were very helpful in advancing the FDIC's thinking and consideration of these challenging issues.

There being no further business, the meeting was adjourned at 3:07 p.m.

Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
and Committee Management Officer
FDIC Systemic Resolution Advisory
Committee

December 10, 2014

Minutes

of

The Meeting of the Systemic Resolution Advisory Committee

of the

Federal Deposit Insurance Corporation

Held in the William Seidman Center

Federal Deposit Insurance Corporation Building

Arlington, Virginia

Open to Public Observation

December 10, 2014 - 9:03 A.M.

I hereby certify that, to the best of my knowledge, the attached minutes are accurate and complete.

Martin J. Gruenberg

Martin J. Gruenberg
Chairman
Board of Directors
Federal Deposit Insurance Corporation