

**STATEMENT OF
FEDERAL DEPOSIT INSURANCE CORPORATION**

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on

**WHO IS TOO BIG TO FAIL? EXAMINING THE APPLICATION OF TITLE I OF THE
DODD-FRANK ACT**

before the

**SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS
COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES**

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Chairman McHenry, Ranking Member Green, and members of the Subcommittee, thank you for the opportunity to testify on behalf of the Federal Deposit Insurance Corporation (FDIC) on Sections 165 and 121 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). Our testimony will focus on the FDIC's role and progress in implementing Section 165, including the resolution plan requirements and the requirements for stress testing by certain financial institutions.

Section 165 of the Dodd-Frank Act

Resolution Plans

Under the Dodd-Frank Act, bankruptcy is the preferred resolution framework in the event of a systemic financial company's failure. To make this prospect achievable, Title I of the Dodd-Frank Act requires that all large, systemic financial companies prepare resolution plans, or "living wills", to demonstrate how the company would be resolved in a rapid and orderly manner under the Bankruptcy Code in the event of the company's material financial distress or failure. This requirement enables both the firm and the firm's regulators to understand and address the parts of the business that could create systemic consequences in a bankruptcy.

The FDIC intends to make the living will process under Title I of the Dodd-Frank Act both timely and meaningful. The living will process is a necessary and significant tool in ensuring that large financial institutions can be resolved through the bankruptcy system.

The FDIC and the Federal Reserve Board issued a joint rule to implement Section 165(d) requirements for resolution plans – (the 165(d) Rule) – in November 2011. The 165(d) Rule requires systemically important financial institutions (SIFIs) -- bank holding companies with total consolidated assets of \$50 billion or more, and nonbank financial companies that the Financial Stability Oversight Council (FSOC) determines could pose a threat to the financial stability of the United States -- to develop, maintain, and periodically submit resolution plans to regulators.

In addition to the resolution plan requirements under the Dodd-Frank Act, the FDIC issued a separate rule which requires all insured depository institutions (IDIs) with greater than \$50 billion in assets to submit resolution plans to the FDIC for their orderly resolution under the Federal Deposit Insurance Act. The 165(d) Rule and the IDI resolution plan rule are designed to work in tandem by covering the full range of business lines, legal entities and capital-structure combinations within a large financial firm.

The 165(d) Rule establishes a schedule for staggered annual filings. The first group of filers -- bank holding companies and foreign banking organizations with \$250 billion or more in non-bank assets (“first wave” filers) -- submitted their initial resolution plans on July 1, 2012. Financial companies with less than \$250 billion, but more than \$100 billion in non-bank assets (“second wave” filers), will file their initial plans by July 1, 2013, and all other bank holding companies – those with assets over \$50 billion – (“third wave” filers) are scheduled to file by December 31, 2013. While the general expectation is that firms will file annually, regulators

may require that a plan be updated on a more frequent schedule, and a firm must provide notice to regulators of any event that may have a material effect on its resolution plan.

Eleven firms comprised the first wave of filers. The nine firms that submitted plans on July 1, 2012, were Bank of America Corporation, Citigroup, JPMorgan Chase, Goldman Sachs, Morgan Stanley, Deutsche Bank, UBS, Credit Suisse, and Barclays. The two other first wave filers, Bank of New York Mellon Corporation and State Street Corporation, submitted plans on October 1, 2012. The second wave filers include Wells Fargo, BNP Paribas, HSBC, and RBS. The third wave filers include approximately 115 firms, the large majority being foreign financial companies conducting business in the U.S.

The 165(d) Rule sets out the information to be included in a firm's resolution plan. The key objectives laid out in the Rule for the initial resolution plans submitted by first wave filers are identifying each firm's critical operations and core business lines, mapping those operations and core business lines to each firm's material legal entities, and identifying the key obstacles to a rapid and orderly resolution in bankruptcy. With regard to key obstacles, these might include such areas as a firm's internal organizational structure, interconnections of the firm to other systemic financial companies, management information system limitations, default and termination provisions of certain types of financial contracts, cross-jurisdictional operations, and funding mechanisms.

The 165(d) Rule provides that smaller, less complex financial institutions subject to the filing requirements may be eligible to file a less detailed, tailored resolution plan, for which the information requirements generally are limited to the firm's nonbanking operations, and the interconnections between the nonbanking operations and its IDI operations.

Section 165(d) of the Dodd-Frank Act requires the FDIC and the Federal Reserve Board to review each resolution plan. If, as a result of their review, the FDIC and the Federal Reserve Board jointly determine that the resolution plan is not credible or would not facilitate an orderly resolution of the firm under the Bankruptcy Code, then the company must resubmit the plan with revisions, including, if necessary, proposed changes in business operations or corporate structure. If the company fails to resubmit a credible plan that would result in orderly resolution under the Bankruptcy Code, the FDIC and the Federal Reserve may jointly impose more stringent capital, leverage, or liquidity requirements; growth, activities, or operations restrictions; or, after two years and in consultation with the FSOC, divestiture requirements.

Federal Reserve Board and FDIC staff reviewed the first wave filers' plans for informational completeness to ensure that all information requirements of the Rule were addressed in the plans. The initial plan submissions for the first wave filers were created using an assumption of the individual firm's failure under "baseline" economic conditions as a starting point. Subsequent submissions are required to take into account "adverse" and "severely adverse" economic conditions.

The eleven firms that submitted initial plans in 2012 will be expected to revise and update their submissions in their subsequent 2013 versions, pursuant to guidance that the FDIC and the Federal Reserve Board will provide to these companies. Resolution plans submitted in 2013 will be subject to informational completeness reviews and reviews for creditability or resolvability under the Bankruptcy Code. Going forward, the FDIC and the Federal Reserve Board expect the revised plans to focus on key issues and obstacles to an orderly resolution in bankruptcy, including global cooperation and the risk of ring-fencing or other precipitous actions. To assess this potential risk, the firms will need to provide a jurisdiction-by-jurisdiction analysis of the actions each would need to take in a resolution, as well as the actions to be taken by host authorities, including supervisory and resolution authorities. Other key issues expected to be addressed in the plans include: the risk of multiple, competing insolvency proceedings; the continuity of critical operations -- particularly maintaining access to shared services and payment and clearing systems; the potential systemic consequences of counterparty actions; and global liquidity and funding with an emphasis on providing a detailed understanding of the firm's funding operations and cash flows.

Stress Testing

Section 165 of the Dodd-Frank Act requires the FDIC to issue regulations for FDIC-supervised banks with total consolidated assets of more than \$10 billion to conduct annual stress tests. The banks must report their respective stress test results to the FDIC and the Federal Reserve Board and these results also are summarized in a public document. The FDIC views the stress tests as an important source of forward-looking analysis that will enhance the supervisory

process for these institutions. Furthermore, these stress tests will support ongoing improvement in a bank's internal assessments of capital adequacy and overall capital planning.

The Dodd-Frank Act requires the FDIC to coordinate with the other supervisory agencies to issue regulations that are consistent and comparable. While each banking agency issued separate final rules with respect to their supervised entities, the final rules were nearly identical across the agencies. The FDIC finalized its rule on annual stress tests on October 15, 2012. Complementing this rulemaking, the FDIC also issued proposed reporting templates that were developed jointly with the other agencies. Lastly, the agencies are working closely on proposed guidance to ensure consistent treatment for all covered financial institutions under the final rule.

Certain insured institutions and bank holding companies with assets of \$50 billion or more comprised the first set of companies to conduct stress tests, which were completed in March 2013. Using September 30, 2012 financial data, institutions developed financial projections under defined stress scenarios provided by the agencies in November 2012. Each company publicly disclosed the results of their stress tests on or before March 31st of this year.

Institutions with assets greater than \$10 billion, but less than \$50 billion, and larger institutions that have not had previously conducted stress tests, will conduct their first round of stress tests later this fall.

Section 121 of the Dodd-Frank Act

Section 121 authorizes the Federal Reserve Board, with the concurrence of two-thirds of the voting members of the Financial Stability Oversight Council (FSOC), to take various actions with respect to a bank holding company with assets of \$50 billion or more or a nonbank financial company supervised by the Federal Reserve Board, if it is determined that company poses a grave threat to the financial stability of the United States. Section 121 also grants the company, upon its request, the opportunity to request a written or oral hearing before the Federal Reserve Board to contest proposed actions.

As a voting member of the FSOC, the FDIC would participate in any discussions involving findings made by the Federal Reserve Board under this section and would carefully weigh the case and its merit in exercising our FSOC vote. To date, the FSOC has not heard any matters involving the use of this “grave threat” authority.

Conclusion

The FDIC has made significant progress in the implementation of Section 165 of the Dodd-Frank Act. Our goal is to ensure that firms that could pose a systemic risk to the financial system develop and maintain resolution plans that identify each firm’s critical operations and core business lines, map those operations and core business lines to each firm’s material legal entities, and identify and address the key obstacles to a rapid and orderly resolution in bankruptcy. Ensuring that any institution, regardless of size or complexity, can be effectively

resolved through the bankruptcy process will contribute to the stability of our financial system and will avoid many of the difficult choices regulators faced in dealing with systemic institutions during the last crisis.