Andrew M. Cuomo
Governor

Benjamin M. Lawsky
Superintendent

February 18, 2014

Via Email to Comment Portal

Mr. Robert E. Feldman
Executive Secretary
Attention: Comments,
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Re: <u>Resolution of Systemically Important Financial Institutions: The Single Point of Entry Strategy</u>

Dear Mr. Feldman:

The New York State Department of Financial Services ("DFS") is pleased to provide the following response to the request by the Federal Deposit Insurance Corporation ("FDIC") for comment on the topic of "Resolution of Systemically Important Institutions: The Single Point of Entry Strategy." (78 Fed. Reg. 76614, December 18, 2013) (the "Comment Request").

In addition to chartering and supervising U.S. institutions that are critical to the financial system infrastructure, DFS licenses, supervises, and regulates more than 100 foreign banking organizations ("FBOs") operating in New York through branches, agencies, and bank subsidiaries, with assets under supervision exceeding $1.8 trillion. These FBOs represent all regions of the globe and embody a range of business models from global systemically important financial institutions ("SIFIs") to smaller and less complex entities. Consequently, DFS has significant experience serving as a host regulator to FBOs and interacting with home country regulators, including on matters relating to resolution planning. These same home country regulators may in turn act as host regulators for U.S. banking institutions. In addition to offering its general support for the single point of entry ("SPOE") strategy, DFS believes that it possesses practical insights from serving as a host regulator for complex FBO's which may provide a useful perspective on the regulatory considerations involved in resolving a SIFI's international operations under a SPOE strategy.

DFS concurs with the FDIC's focus on developing a SPOE strategy to carry out the resolution of a SIFI and views the FDIC's work in this regard as an important contribution to ending "Too Big To Fail." However, in order to be workable, a global resolution strategy must be structured to accommodate the supervisory concerns of host country regulators who would likely engage their supervisory authority in the period prior to a resolution to protect the interests of domestic creditors and depositors.

Since DFS has experience as a host regulator for FBOs, we have thought it useful to highlight selected practical challenges that a host regulator may have to consider when a SPOE resolution strategy is proposed, especially since a host regulator's supervisory actions during the run-up to a possible resolution may affect the successful implementation of a SPOE strategy. The first step toward meeting these challenges for the home supervisor is gaining an understanding of host jurisdiction authority and requirements; building an effective working relationship with host country regulators; and endeavoring to coordinate regulatory preparations with the host authorities long before a decision on resolution is required.

Single Point of Entry Strategy

DFS concurs with the FDIC's focus on implementing its Dodd-Frank Act Title II authority through development of a SPOE strategy for the resolution of U.S. SIFIs, including those that may have significant international operations. Adoption of such a strategy for resolution of a SIFI will generally promote stability in the U.S. financial system. For similar reasons, it will also promote global stability for those U.S. SIFIs that are significantly active internationally. In preparation for a SPOE strategy, key international branches and entities must be identified not only for the purposes of assessing the SIFI's global stability, but also to preserve the franchise value of the U.S. SIFI.

International Operations of a SIFI

In order for the resolution planning process to be effective, it should be based on a recognition by the home supervisor that the regulatory and supervisory framework of host country regulators reflect their jurisdictions' legitimate interests. Therefore, understanding those frameworks is a key to understanding a SIFI's international operations and thus developing an effective SPOE strategy. Federal regulators should have a good understanding of the requirements the host regulators may place on the SIFI's important international operations. The areas of understanding should include: 1) any statutory mandate that would require the host country regulators to act (i.e., "hard triggers") in a manner that might jeopardize the plan's success, or relatedly, what actions on the part of the SIFI or home country regulator may give the host country authorities sufficient comfort for forbearance; 2) the range of supervisory tools (such as imposing capital, liquidity, asset maintenance and risk governance requirements at the local entity level) that could be employed by the host country regulator over the continuum of recovery efforts through to a final resolution decision; 3) local laws and regulations regarding funding and credit limits; and 4) any information sharing mechanism between the host regulator and the U.S. federal regulators.

It must be recognized that the various host regulators are not necessarily making their resolution decisions locally at the same time the home regulator's decision for SPOE resolution of the overall organization is made. In fact, it is likely that the SPOE decision will be made and the host regulators will be asked to forebear on their individual resolution authority in the attempt to avoid an uncoordinated resolution at multiple points of entry, where host authorities independently resolve the operations within their jurisdictions locally. However, in order to forebear, it is likely that a host regulator will engage the supervisory tools at its disposal at increasing degrees, which conceivably could cause shifts in assets, liquidity, and capital within the SIFI organization that could impede a planned resolution. Therefore, it is recommended that

U.S. SIFIs "stress-test" for host regulator supervisory tools to determine the point at which decision-making processes may be influenced and whether the success of the resolution plan may be impeded by host country measures.

Organizational Structure of International Operations

The Comment Request seeks comments on, among other things, the potential advantages or disadvantages for the resolvability of a SIFI of a requirement that SIFIs conduct their international operations through subsidiaries. Specifically, it asks whether a subsidiarization requirement for foreign operations would reduce the likelihood of ring-fencing by host country regulators and improve the resolvability of a SIFI.

From a business perspective, subsidiarization would require that each entity in the SIFI group separately hold sufficient capital to fund its operations. The required separate capitalization of each subsidiary provides less flexibility for the organization. Capital, or excess levels of capital, may become trapped in a given jurisdiction and may not be able to be quickly redeployed within the organization to facilitate the execution of its recovery plan and avoid a resolution.

From an overall regulatory perspective, it is within a host country's authority to mandate a particular type of entity structure, and such mandates by a host regulator are likely to be related to the specifics of its legal and regulatory system, including its approach to resolving local operations. From the DFS perspective as a host regulator to FBOs, New York State allows FBOs to establish branches and bank subsidiaries within its borders, with a branch being the structure of choice for the vast majority of FBOs. While NYS Banking Law allows an FBO to choose from a variety of entry structures (representative office, agency, branch, or subsidiary bank), the license application process confirms that the structure selected is compatible with the business model of operations contemplated within New York State. For New York, at least, the selection of an entity structure is a business decision of the FBO and not driven by local resolution requirements.

However, regardless of the type of entity an FBO selects for its New York State operations, DFS has various supervisory tools that can be engaged for an orderly resolution of local operations. Although the branch lacks capital, there are supervisory tools that can be utilized to protect the branch's third-party liabilities holders, such as requiring maintenance of a "Due To" position and/or maintenance of local assets.

While certain of these host regulator supervisory tools might be thought of as forms of "ring fencing," it is important to distinguish between supervisory tools that can be employed in varying degrees and at different times as a matter of supervisory discretion, in order to protect local stakeholders from being disadvantaged by a home country initiated resolution process, and tools that, once deployed, have fixed and uncontrollable consequences. New York's willingness to allow FBOs the flexibility to enter the state through a variety of structures is predicated on DFS' ability to have full access to its supervisory and regulatory tool box in a potential recovery or resolution scenario.

A rather different aspect of subsidiarization relates to the costs and benefits of subsidiarizing back office and other shared intra-institutional support services. We perceive broad agreement among larger domestic and foreign institutions that this type of subsidiarization is a desirable step to facilitate recovery and resolution planning. The centralization of support services into a subsidiary benefits a resolution scenario in the following manner: 1) select business lines that rely on the support functions may be sold without the associated functions, thereby limiting overall service disruption to the remaining organization; 2) once the select business lines are sold, the SIFI could conceivably continue back-office servicing for the buyer to generate a separate revenue stream in resolution; and 3) the support subsidiary itself can be sold as an outsourcing platform.

Bridge Financial Company

Over the years, DFS has had the opportunity to work with home country regulators that have proposed resolution scenarios involving various types of organizations, such as bridge holding companies, bridge banks, and bail-ins. As a host regulator, DFS would like to offer its observations on the challenges presented by "bridge organizations.”

One point worth noting is that under the regulatory schemes of some jurisdictions, a "bridge organization" instituted at the holding company level might well be considered as involving a change of control/change of management/change of guarantor of the operating entities. In addition to any legal and contractual consequences that might flow from that characterization, it could require that the bridge organization apply for and receive a separate regulatory approval or license to conduct a banking business in those jurisdictions, and the operating subsidiaries in those jurisdictions may be required by host country rules to provide notices and make appropriate filings.

Assuming regulatory receptivity to the bridge organization, the application process should be relatively swift and benign in most host jurisdictions. However, since time will be of the essence at the point of resolution, gaining familiarity in advance with host jurisdictions’ application and approval process will be important. The SIFI itself is most familiar with the requirements within the host jurisdictions where it operates. Therefore, it is recommended that covered institutions (SIFIs) obtain and keep current information about the necessary application and approval process of the host countries where they operate. A covered institution could incorporate the information or documentation required by host country regulators within its Recovery and Resolution Plan (RRP) filings.

The resolution process may also benefit from the inclusion of advanced preparation of application material and a review of host country law and regulations to determine if any changes to law and regulations would be helpful in accommodating an expedited approval process. There may also be an opportunity for home and host country regulators to take steps in advance to streamline the application process for a resolution scenario.

Based upon the description of the "Bridge Financial Institution" within the Request for Comment, our understanding is that it is expected that 100% of the foreign operations of the SIFI will be transferred into the Bridge Financial Institution, since the resolution will be occurring at the highest holding company level. However, if this is not the case and certain portions of the international operations would be left behind, the viability of that portion may be questionable and be problematic for the host jurisdiction, possibly to the point of jeopardizing the success of the overall plan in achieving financial market stability.

Communication Plan

An effective SPOE strategy must, of course, include an effective communication plan. In order to have an effective communication plan for a SPOE strategy for a SIFI with international operations, it must also proactively address the legitimate concerns of consumers and other constituencies in host countries. While prompt, clear and straightforward communication with host regulators having responsibility for the SIFI's significant overseas operations is obviously essential, an effective plan should take into consideration the possibility that while a SIFI's operations in a particular country may not be significant to recovery or resolution of the SIFI overall, such operations may be systemically important to the host country's economy, especially if the operations are retail in nature and/or if the country is an emerging market. In these circumstances, news of a resolution plan that is not quickly and carefully communicated could conceivably lead to a run on the SIFI's local operations in a host country. News of such an event in one jurisdiction could quickly have a negative impact on the broader plan for resolution based on a SPOE strategy.

Conclusion

DFS appreciates the opportunity to comment on the FDIC's proposed SPOE strategy. In principle, we support the FDIC's focus on developing a SPOE strategy as the principal option for the resolution of most U.S. SIFIs. The SPOE approach should generally promote both U.S. financial system stability and global stability for those U.S. SIFIs that have international operations.

DFS would be pleased to provide additional information and participate in further discussions to assist the FDIC in understanding the perspective on global resolution strategy that DFS has developed as a host regulator overseeing the operations of FBOs within New York State.

Sincerely,

Benjamin M. Lawsky
Superintendent of Financial Services