Vanguard®

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Federal Deposit Insurance Corporation
Attn: Robert E. Feldman
Executive Secretary
550 17th Street, NW
Washington, D.C. 20429

November 8, 2010

Via Electronic Submission

Re: Notice of Proposed Rulemaking Implementing Certain Orderly Liquidation Authority Provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act

Dear Mr. Feldman:

We appreciate the opportunity to comment on the Notice of Proposed Rulemaking Implementing Certain Orderly Liquidation Provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Notice"). Vanguard[1] is an SEC-registered investment advisor with approximately $1.5 trillion in assets under management. On behalf of Vanguard, and, in particular, the individuals and families who invest in our funds, we commend the Federal Deposit Insurance Corporation ("FDIC") for addressing concerns regarding provisions in the Dodd-Frank Act (the "Act") that appear to give the FDIC discretion to treat similarly situated creditors of a systemically important institution inequitably. The clarification provided by the proposed rules (the "Proposed Rules") will bring a measure of comfort to creditors of institutions that could fall under the purview of the FDIC's new orderly liquidation authority. Separately, we continue to have some concerns about the impact of the FDIC's insolvency regime on financing costs and market volatility which, as explained below, we hope will be clarified in further FDIC and other rulemaking. Finally, we believe certain provisions of the Proposed Rules require additional clarification, including careful reconsideration of provisions that would value certain collateral underlying secured transactions at par.

[1] Vanguard offers more than 160 U.S. mutual funds and serves approximately 23 million shareholder accounts.

Treatment of Similarly Situated Creditors

As we expressed in our May 2010 letter to Senators Dodd and Shelby, [2] certain language in the Act appears to permit the FDIC, in its sole discretion, to pay those holding identical bonds differing amounts. Specifically, language in those provisions entitled "Creditors Similarly Situated," "Additional Payments Authorized," and "Equitable Treatment of Similarly Situated Creditors"[3] permit "additional payments" to be made to certain creditors where such payments are necessary to maximize value and minimize losses in liquidation, while avoiding a disorderly collapse. Such an insolvency regime, however, would be highly subjective and would be inconsistent with the proper and historic structure and function of the nation's financial markets, and would contravene investors' reasonable expectations of due process under the U.S. Bankruptcy Code. The resulting uncertainty could lead to creditors abandoning "too big to fail" institutions at the first sign of difficulty, injecting new risks, costs, and volatility into the financial markets.

We believe, however, that the Proposed Rules adequately clarify and properly limit the FDIC's discretion to pay certain creditors more in a liquidation scenario. By specifically excluding holders of long-term senior debt, subordinated debt, and equity interests from eligibility for "additional payments," such creditors have explicit assurance that they will not be treated differently than others similarly situated. Payments will instead be limited to certain short-term creditors, including those employees necessary to continue operations during the receivership. To ensure that additional payments to eligible creditors are not made arbitrarily, the Proposed Rules require that such payments be evaluated on a case-by-case basis, meet strict statutory standards intended to achieve the goals of the receivership, and may only be made after a vote of the full FDIC Board. Finally, the Act itself requires all creditors of a class to receive no less than what they would have received in Chapter 7 liquidation. This framework, we believe, strikes the appropriate balance of ensuring fair treatment of creditors while maximizing the value of the liquidation, and brings the resolution authority granted to the FDIC under the Act in line with investor expectations under established insolvency regimes.

Although the Proposed Rules, if approved, would bring clarity as to how similarly situated creditors will be treated under the orderly liquidation authority, we continue to have some general concerns about the effect of this insolvency regime from a market perspective. The Act permits the FDIC to seize an institution "in default or in danger of default," as opposed to bankruptcy law, which requires a company to be in default. As long-term and subordinated debt and equity holders will expect to incur significant losses under the orderly liquidation authority, such creditors and investors may be likely to sell their interests at the first sign of difficulty. This could increase financing costs for companies that may fall under FDIC receivership, increase market volatility, and lead to an acceleration of the very situation that the Act seeks to avoid. We expect, however, that recent requests for comments by the Financial Stability Oversight Council ("FSOC") and subsequent rulemaking will bring clarity as to which institutions could be covered by this regime.[4] The FSOC's proposals, coupled with the Proposed Rules, should bring additional certainty to the market regarding the operation of the FDIC's orderly liquidation authority.

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[2] *See* Letter from George U. Sauter, Chief Investment Officer of Vanguard, to The Honorable Christopher J. Dodd and The Honorable Richard C. Shelby, May 4, 2010.
[3] *See* Sections 210(b)(4), 210(d)(4), and 210(h)(5)(e) of Title II, respectively.
[4] *See* Advanced Notice of Proposed Rulemaking Regarding Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies, FSOC 2010-0001-0001, October 1, 2010.

Valuation of Certain Collateral Underlying Secured Transactions at Par

Section 380.2(c) of the Proposed Rules would require that the FDIC value collateral underlying certain short-term secured financings at par if the collateral consists of U.S. Treasury or other government securities. While this provision is intended to encourage lenders to request only high-quality, liquid securities as collateral for such financings, it may lead to unintended effects on this market. For example, U.S. Treasury or other government securities may trade at a premium. Valuation of these securities at par would leave certain creditors under-secured in a liquidation scenario. The possible loss in value to these creditors may, contrary to the FDIC's intent, discourage the use of such high-quality collateral. If the securities are trading at a discount, both parties may be incentivized to under-collateralize, as a creditor would be assured of receiving par if the counterparty falls under the receivership of the FDIC. The assurance of receiving par could also have a wider effect in the repo market, as lenders may become comfortable with collateral that they would not otherwise accept. In order to avoid these unintended consequences, we urge the FDIC to instead provide that all collateral will be valued at its fair market value. This approach would help achieve the FDIC's goals without injecting new uncertainty into a market with otherwise well-defined parameters for the valuation of eligible collateral.

Additional Clarification

Finally, we believe that certain provisions of the Proposed Rules require additional clarification. We ask for clarification as to whether Section 380.2(c) is intended to apply solely to repurchase agreements, or to other types of collateralized transactions as well. The discussion in the Notice appears to focus on the repo market, however, the provision as drafted could be interpreted to apply to other types of secured transactions.[5] We recommend that this provision be limited to repo. If it is the FDIC’s intent to apply this provision beyond the repo market, we request that the scope of its application be clearly identified so that the potential effects on other types of secured transactions can be accurately assessed. Further, we ask that the FDIC indicate how, and as of which date, it will determine the value of the collateral under this provision. We recommend that the value of the collateral be determined on the date on which the FDIC is appointed receiver; any shortfall in the collateral value relative to the value of the cash borrowed would then be fixed as an unsecured claim of that creditor. Finally, the FDIC should provide guidance as to how it will determine the amount that a creditor would otherwise receive under a Chapter 7 liquidation. Although creditors are assured of such a minimum recovery, it is not clear under the Act or the Proposed Rules as to how such a recovery would be calculated. Understanding this process will be critical to the ability of market participants to accurately evaluate how creditors will be treated under the FDIC’s orderly liquidation framework.

[5] *See* Notice, page 11.

We thank the FDIC for providing us with the opportunity to share our thoughts on the Notice and Proposed Rules. If you have any questions about Vanguard's comments or would like any additional information, please contact Natalie Bej, Principal, at (610) 503-5693 or Nathan Will, Associate Counsel, at (610) 669-2689.

Sincerely,

/s/ Gus Sauter

Managing Director
and Chief Investment Officer
Vanguard

cc: The Honorable Sheila C. Bair, Chair, Federal Deposit Insurance Corporation
Financial Stability Oversight Council