THE FINANCIAL SERVICES ROUNDTABLE

Financing America's Economy

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

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

File Number: FR Doc. 2010-26049

Ladies and Gentlemen:

The Financial Services Roundtable (the "Roundtable")[1] appreciates the opportunity to provide the Federal Deposit Insurance Corporation (the "FDIC") with its comments regarding implementation of certain elements of Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"),[2] as set forth in the FDIC's Notice of Proposed Rulemaking published in the Federal Register on October 19, 2010 (the "FDIC Comment Request").[3]

The Roundtable is composed of large, integrated financial services companies who finance most of the nation's economy and are critical to its sustained growth. The Roundtable strives be the premier executive forum for the leaders of the financial services industry, to lead in industry best practices, and to provide a positive industry perspective on legislative and regulatory policy. The Roundtable believes the competitive marketplace should largely govern the delivery of products and services, and that regulation should mitigate systemic risk and enhance financial stability.

The Roundtable fully supports the FDIC's goals of issuing implementing regulations under Title II that provide transparency, market certainty and appropriate flexibility to address the "Too Big to Fail" dilemma and achieve financial stability. This letter focuses

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[1] The Financial Services Roundtable represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Roundtable member companies provide fuel for America's economic engine, accounting directly for $74.7 trillion in managed assets, $1.1 trillion in revenue, and 2.3 million jobs.

[2] Pub. L. No. 111-203, § 201 et seq., 124 Stat. 1376 (2010).

[3] 75 Fed. Reg. 64173 (October 19, 2010).

on the proposed rules and the FDIC's related questions for which a response is due by November 18, 2010. The Roundtable also will submit a supplemental response to the broader questions raised in the FDIC's Comment Request for which comments are due on January 18, 2011.

Title II's Orderly Liquidation Authority ("OLA") is a powerful set of statutory provisions that potentially apply to the failure of U.S. bank and thrift holding companies, U.S. nonbank systemically significant financial companies, and subsidiaries of companies "predominantly engaged" in financial activities.[4] Congress sought to ensure that the FDIC would implement the OLA in a "manner that mitigates [systemic] risk and minimizes moral hazard"[5] to the greatest extent possible. Even if the OLA is designed for emergencies and will rarely be invoked, the rules promulgated by the FDIC that implement OLA will have a dramatic effect on the manner in which systemically important financial institutions ("SIFIs") structure their operations, do business with counterparties, and access credit. Because of this profound effect, the FDIC should pursue a rulemaking process that provides SIFIs with significant clarity, transparency, and settled expectations. Thus, the Roundtable favors a careful and iterative rulemaking process by the FDIC in implementing Title II, one that favors deliberation and precision over speed.

In this regard, the Roundtable strongly urges the FDIC to extend the comment period to the proposed rules and to address the elements of this proposal in the context of the broader rulemaking that the FDIC intends. This is necessary because of the sensitivity and complexity of the topics, the potential for unintended consequences and the connection and interdependence between the proposal with the balance of the FDIC's rulemaking.

Our specific comments follow regarding the current proposed rules and the FDIC's related questions.

Section 380.2(a)-(b) – Limitations on Additional Payments to Creditors

Proposed Section 380.2, which identifies certain categories of creditors who will never satisfy the requirements for receiving "additional payments" in the event of an orderly liquidation is inappropriately restrictive and should be withdrawn. A rule that restricts the situations in which the FDIC may exercise its authority to provide additional payments may prevent it from taking actions that might maximize the value of assets of the financial company being liquidated and "mitigate[e] potential adverse effects on the financial system."[6] Thus, rather than impose a blanket prohibition on additional payments to an entire class of creditors, the FDIC should exercise discretion under Sections 210(b)(4), (d)(4), and (h)(5)(e) to provide additional payments on a case-by-case basis for all classes of creditors.

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[4] Section 201(a)(11) of the Dodd-Frank Act, *codified at* 12 U.S.C. § 5381.

[5] 75 Fed. Reg. 64174, 64175 (October 19, 2010) (citing § 204 (a) of the Dodd-Frank Act).

[6] Section 203(b)(5) of the Dodd-Frank Act, *codified at* 12 U.S.C. 5383.

It is impossible to predict every circumstance surrounding a particular liquidation. As the FDIC itself notes, "the ability *to act quickly and decisively* has been found to reduce losses to the deposit insurance funds . . . *and it is expected to be equally crucial in resolving non-bank financial firms under the Dodd-Frank Act*."[7] The proposed rule may restrict the FDIC's ability to act quickly (by requiring a vote by the FDIC's board of directors) and decisively (by stating that certain categories of creditors will never qualify for additional payments). Moreover, the creation of a bright line between creditors who will never receive additional payments and those that may (albeit under restricted circumstances) could cause market participants to structure their relationships, in an attempt to achieve what may be perceived as potentially more beneficial treatment in an OLA proceeding. Systemic risk may be reduced by encouraging institutions to rely more on longer term debt generally, but the proposed rule would not support this approach.

The Roundtable believes it is crucial that the FDIC avoid creating a bright line that will both distort credit markets and potentially restrain the FDIC from taking desirable and even necessary actions in a crisis. A rule categorically ruling out additional payments to longer-term debt holders could discourage such debt, which might otherwise reduce systemic risk and enhance liquidity. The Roundtable thus urges the FDIC to withdraw these provisions providing limitations on its ability to permit additional payments.

If the FDIC nonetheless decides to maintain this approach, the Roundtable offers the following comments in response to the questions the FDIC asked regarding Section 380.2(a)-(b).

1. Should "long-term senior debt" be defined in reference to a specific term, such as 270 or 360 days or some different term, or should it be defined through a functional definition?

If the FDIC continues to follow this approach, the Roundtable asks the FDIC to use a narrow definition of those creditors who will not be available to receive additional payments, *e.g.* by focusing not on a specific term of an instrument but instead on certain qualifying regulatory capital instruments. Holders of capital are aware that their claims are intended to be satisfied only after those of other creditors. Therefore a rule disadvantaging the holders of these instruments would likely less adversely affect the market for such instruments than would the proposed rule, and would reduce the potential adverse effect on the funding profiles of SIFIs. In addition, while the Roundtable does not believe that the FDIC should adopt any rule based on the term of the instrument, we note that the current proposal is vague as to the manner in which a term-based rule would apply. If maintained, the rule should be revised to clarify that the relevant term of an instrument is its remaining term. A rule based on any other metric risks creating significant uncertainty among SIFIs and their creditors.

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[7] 75 Fed. Reg. at 64176 (emphasis added).

2. Is the description of "partially funded, revolving or other open lines of credit" adequately descriptive? Is there a more effective definition that could be used? If so, what and how is it more effective?

If the FDIC continues to follow this approach, the Roundtable urges the FDIC to continue to protect "lines of credit that are necessary to continuing operations essential to the receivership or bridge financial company,"[8] as in its proposed rule. In addition, the FDIC should clarify that "open lines of credit" will be protected without regard to the term of such lines of credit. Such clarification would help to avoid the possibility that essential credit facilities that are "functionally" short-term (i.e. facilities that allow the covered financial institution to maintain liquidity on a daily, intraday, or weekly basis) will be considered "long-term senior debt" for purposes of Title II.

3. Should there be further limits to additional payments or credit amounts that can be provided to shorter term general creditors? Are there further limits that should be applied to ensure that any such payments maximize value, minimize losses, or are to initiate and continue operations essential to the implementation of the receivership or any bridge financial company? If so, what limits should be applied consistent with other applicable provisions of law?

The Roundtable urges that no additional such limits be imposed. As noted above, the Roundtable believes that these proposed rules and other related ones should be considered in connection with broader issues in the OLA rulemaking. For example, uncertainty may result from the lack of clarification as to how the FDIC will determine which contracts enter the bridge financial company in the first place, [9] or the circumstances under which additional payments to creditors will be "clawed back" under Section 5390(o)(1)(D), and how both of these situations interact with the current proposed rules. These are examples of why we believe it is important that the FDIC consider all of the components of the provisions implementing the OLA subject to a common comment period.

4. Under the Proposed Rule, the FDIC's Board of Directors must determine to make additional payments or credit amounts available to shorter term general creditors only if such payments or credits meet the standards specified in 12 U.S.C. 5390(b)(4), (d)(4), and (h)(5)(E). Should additional requirements be imposed on this decision-making process for the Board? Should a super-majority be required?

The Roundtable urges that no additional limits be applied to these circumstances, which are already appropriately limited in the Act.

<u>Section 380.2(c) – Valuation of Collateral</u>

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[8] 75 Fed. Reg. at 64181.

[9] Section 210(h)(1)(B) of the Dodd-Frank Act, *codified at* 12 U.S.C. § 5390.

5. Under the Dodd-Frank Act, secured creditors will be paid in full up to the extent of the pledged collateral and the proposed rule specifies that direct obligations of, or that are fully guaranteed by, the United States or an agency of the United States shall be valued for such purposes at par value. How should other collateral be valued in determining whether a creditor is fully secured or partially secured?

6. During periods of market disruption, the liquidation value of collateral may decline precipitously. Since creditors are normally held to a duty of commercially reasonable disposition of collateral [Uniform Commercial Code], should the FDIC adopt a rule governing valuation of collateral other than United States or agency collateral? Would a valuation based on rolling average prices, weighted by the volume of sales during the month preceding the appointment of the receiver, provide more certainty to the valuation of other collateral? Would that help reduce the incentives to quickly liquidate collateral in a crisis?

Proposed Rule Section 380.2(c) states that

> "[P]roven claims secured by a legally valid and enforceable or perfected security interest or security entitlement in any property or other assets of the covered financial company shall be paid or satisfied in full to the extent of such collateral, but any portion of such claim which exceeds an amount equal to the fair market value of such property or other assets shall be treated as an unsecured claim and paid in accordance with the priorities established in 12 U.S.C. § 5390(b) and otherwise applicable provisions."[10]

The Roundtable notes that this proposed rule fails to specify a timing point for determining the value of collateral of a secured claim or other important related issues regarding the process and mechanisms for such valuations. We again urge the FDIC to postpone finalization of the proposed rule until it can be considered in the context of the entirety of the OLA implementing regulations.

The proposed rule provides no indication as to whether the determination of the "fair market value" of collateral will be based on the value of the collateral at the time the FDIC was appointed receiver, at the time the collateral was sold, or at some other reference point. As a general matter, the Roundtable urges the FDIC to propose an approach that mirrors Sections 363(k) and 506 of the Bankruptcy code, and to include the ability of a creditor to make a credit bid for the collateral at the FDIC's valuation. This would reduce the creditor's claim by the amount of the valuation, provided that the collateral is turned over to the creditor. If the FDIC determines that the collateral cannot be sold, there should be a specified procedure for disputing the valuation and obtaining a judicial determination of any dispute during the administrative claims process.

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[10] 75 Fed. Reg. at 64181.

Concerns about clear rules are particularly acute in the context of collateralized short term lending, for as the FDIC itself notes, a financial company can fail precisely because short term creditors lack sufficient information as to the quantity and value of collateral.[11] A proposal with greater clarity as to valuation timing, process and metrics for secured claims will assure creditors of a financial institution that in the event of a liquidation they will have greater certainty as to how their claims will be valued, and that the value placed on their collateral will be in line with the fundamental value of the collateral.

For these reasons, the Roundtable asks that the FDIC refrain from finalizing these regulations until such time as it has also proposed and received comment on other related OLA regulations.

Section 380.2(c) – Valuation of U.S. Government Obligations at Par

Proposed Rule Section 380.2(c) also states that

> "Proven claims secured by . . . security interests or security entitlements in securities that are direct obligations of, or that are fully guaranteed by, the United States or any agency of the United States shall be valued for such purposes at par value."[12]

The Roundtable urges the FDIC, at a minimum, to provide further clarification regarding the meaning of this proposal. First, there is some ambiguity, which should be clarified; as we understand it, "par value" here refers to the described collateral, not the claim. Second, it is unclear if valuing such collateral at par value would act as a "floor" or "ceiling" for valuation purposes if the fair market value of the collateral was either above or below its par value. Moreover, if the intention is to encourage the use of U.S. government obligations as collateral, we urge the FDIC to clarify that intention and explore ways to achieve that goal in a more extended comment process that can consider potential unintended consequences. More importantly, we urge the FDIC not to implement a rulemaking as to favored or disfavored types of collateral, but instead to rely on a general fair valuation mechanism. This would allow the FDIC to maintain the flexibility required for optimal implementation of Title II, and will allow market mechanisms to determine which collateral arrangements are most advantageous for risk mitigation.

Section 380.3 – Personal Services Agreements

The proposed rules provide that personal services agreements with certain officers and directors would not be covered by the provisions of Section 380.3(b) that state that where the FDIC accepts such personal services prior to repudiation. It would be bound by the agreement with respect to pre-repudiation services and treat payments due for such services as administrative expenses under Title II. The Roundtable is concerned that carving out such agreements from the coverage of Section 380.3(b) may interfere with the

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[11] 75 Fed. Reg. at 64178 ("A major driver of the financial crisis . . . was in part due to an overreliance . . . on funding . . . using volatile, illiquid collateral . . .").

[12] 75 Fed. Reg. at 64181.

ability of the FDIC to retain important executives in the event of a Title II process and thus impair maximizing the value of the company and financial stability.

Section 380.5, 380.6 – Insurance Companies

The Roundtable urges the FDIC to provide further clarification regarding some of the proposed rule's discussion with respect to insurance companies. Specifically, the Roundtable requests that the FDIC clarify that (i) Congress did not intend Title II to apply to insurance companies already subject to resolution authority under state law, and (ii) in the event that that an insurance company is part of a holding company or other corporate structure that is liquidated under Title II, the resolution of the insurance company will be conducted separately, under established state insurance law regulatory regimes by the relevant state insurance regulator appointed as rehabilitator or liquidator by the applicable state court.

First, some language in the proposal could be read to suggest that the FDIC under Title II may conduct a liquidation or rehabilitation of an insurance company under Title II. The preamble to the proposed rule states that "either" a State regulatory agency or the FDIC has the authority to liquidate a covered insurance company under Title II.[13] The Roundtable believes that the FDIC's intent was to clarify the FDIC's view that it could be appointed under applicable state insurance laws to conduct a liquidation or rehabilitation of an insurance company, but only as permitted and provided for under applicable state insurance laws. Title II itself does **not** provide the FDIC with such authority.

Even if the FDIC were to act as provided under Title II to "stand in the place of the appropriate regulatory agency and file the appropriate judicial action in the appropriate State court to place such company into orderly liquidation under the laws and requirements of the State,"[14] the Dodd-Frank Act only authorizes the FDIC to "file" such a proceeding, not to conduct such a liquidation or rehabilitation. Under applicable state insurance laws, which are in no way displaced by the Dodd-Frank Act in this respect, that process should still be conducted by the state insurance regulator appointed as rehabilitator or liquidator by the applicable state court. We ask that the FDIC clarify that the FDIC's authority under Section 203(e)(3) is limited to filing a petition when the state insurance regulator fails to act in a timely fashion and that, upon granting of any such petition, the state insurance regulator, as required by state insurance law, will be designated rehabilitator or liquidator by the applicable state court. Put another way, the result of the FDIC "filing" such a proceeding in state court under Section 203(e)(3) is to "place such company into orderly liquidation under the laws and requirements of the State" and, under state law, such placement results in appointment of the state insurance regulator, not the FDIC, as rehabilitator or liquidator. Nothing in Section 203(e)(3) suggests otherwise.

[13] 75 Fed. Reg. at 64179.

[14] Section 203(e)(3) of the Dodd-Frank Act (emphasis added).

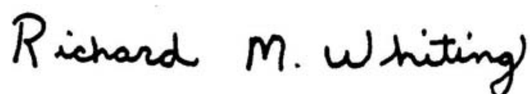
Second, the proposed rule contemplates that "proceeds from liens taken on assets of covered financial companies that are insurance companies or covered subsidiaries of insurance companies" under Section 380.6 could extend to unencumbered assets of the insurance company, particularly assets that would satisfy the policyholders of the insurance company in the event of a liquidation. The Roundtable understands section 380.6 to state that the FDIC will take liens on the assets of an insurance company or covered subsidiary of an insurance company only to the extent that funds were actually extended to such an entity. The Roundtable requests that the FDIC clarify that Title II only affords the FDIC the ability to take liens on an insurance company or covered subsidiary to cover loans the FDIC has already extended to such entities.

Conclusion

The Roundtable expresses its appreciation to the FDIC for its leadership in the Title II rulemaking process. The Roundtable looks forward to a thorough and constructive dialogue with the FDIC as the rulemaking process continues. We also appreciate the FDIC's openness to comment and willingness to work with the public and stakeholders in implementing the OLA. The Roundtable will continue to strive to be a positive voice for the financial services industry in this process.

The Financial Services Roundtable thanks the FDIC for the opportunity to comment on the proposed rule. If you have any questions, please feel free to contact me or Brian Tate at (202) 289-4322.

Sincerely,



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