



April 19, 2013

Mr. Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, DC 20429

Attention: Comments
Email: Comments@FDIC.gov

Re: Notice of Proposed Rulemaking –
“Deposit Insurance Regulations; Definition of Insured Deposit”
RIN 3064-AE00

The American Bankers Association (ABA)¹ and the ABA Securities Association (ABASA)² appreciate the opportunity to comment on the Notice of Proposed Rulemaking by the Federal Deposit Insurance Corporation (the FDIC) concerning “Deposit Insurance Regulations; Definition of Insured Deposit” (the Proposal).³ As we explain more fully below, we urge the FDIC to combine the deposit insurance determination in the Proposal with a determination that foreign deposits in overseas branches of U.S. banks are “deposit liabilities” for purposes of depositor preference. This step would best meet the requirements of the U.K. regulators and of the banking industry and its customers without extending FDIC deposit insurance coverage beyond the intentions expressed by the FDIC in offering its Proposal.

¹ The American Bankers Association represents banks of all sizes and charters and is the voice for the U.S. \$14 trillion banking industry and its 2 million employees. The ABA’s extensive resources enhance the success of the nation’s banks and strengthen the U.S. economy and communities.

² ABASA is a separately chartered affiliate of ABA, representing those holding company members of ABA that are actively engaged in capital markets, investment banking and broker-dealer activities. ABASA members also generally have more international operations than their counterparts in ABA, including many with full service branch, bank and capital markets operations in several jurisdictions outside the United States.

³ 78 Fed. Reg. 11,604 (Feb. 19, 2013).

I. Introduction and Executive Summary

U.S. banks that have overseas offices and the regulators of those banks are facing a significant challenge created by the differential treatment of foreign depositors under U.S. law in connection with the failure and subsequent liquidation of a U.S. bank. Under an Advisory Opinion provided by the FDIC's Acting General Counsel in 1994, the preference for "deposit liability" claims under the so-called "depositor preference" statute⁴ enacted in 1993 was interpreted as excluding deposit claims solely payable in a foreign branch of a U.S. bank. The subordination of such claims has long created tension with foreign regulators, but as a result of concerns stemming from the recent international financial crisis it has led to direct challenges to the banking operations of U.S. banks in the United Kingdom and will, we believe, lead to similar challenges in other countries, unless cured.

Based on the discussion in the preamble of the Proposal, the FDIC appears to believe that the Proposal's rejection of insurance for dually payable foreign deposits⁵ adequately addresses this international dilemma. In addition, the FDIC stated that the Proposal more generally, "would address several key concerns: (1) Maintaining public confidence in federal deposit insurance; (2) protecting the [Deposit Insurance Fund]; (3) ensuring that, in the event of an insolvency, the FDIC is in a position to administer the resulting receivership effectively and fairly; and (4) enhancing international cooperation."⁶ We and our member banks share all of these objectives with the FDIC.

Unfortunately, we cannot agree that the Proposal has fully or adequately resolved all the important issues involved with accomplishing these important goals. The Proposal fails to address the depositor preference issue directly, and all of the challenges identified in this letter stem from this one significant omission. In essence, the Proposal is limited to an interpretation that foreign, dually payable deposits will not be covered by FDIC deposit insurance. This interpretation does not cure the subordination of foreign depositors and therefore does not solve the underlying issue raised by international regulators, including the U.K. Financial Services Authority (the UK FSA).⁷

On the contrary, the interpretation only assumes that banks may make foreign deposits dually payable at a U.S. office as a potential option for addressing the depositor preference issue. The interpretation does not address any of the costs, risks, or complexities of instituting dual payability, other than attempting to resolve the question of whether or not such deposits are insured by the FDIC. As we discuss below, while making foreign deposits dually payable may

⁴ 12 U.S.C. § 1821(d)(11).

⁵ In this letter, "dually payable," "dual payability" and "dual pay" all refer to foreign deposits that meet the standard in 12 U.S.C. § 1813(l)(5)(A) and are contractually payable also at "an office of the depository institution located in any State."

⁶ 78 Fed. Reg. at 11,607.

⁷ We note that, as of April 1, 2013, under U.K. law, the UK FSA's responsibilities have been allocated to the Prudential Regulation Authority and the Financial Conduct Authority. However, for convenience, we will continue to refer to the UK FSA throughout this comment letter.

place them on par with uninsured domestic deposits under U.S. law, it creates potential interpretive issues and may not be recognized by all jurisdictions as an acceptable solution to the issue of foreign depositor subordination. The need for clarity and certainty is paramount, as non-U.S. regulators are likely to require definitive evidence and opinions that the subordination of their depositors has been cured.⁸

More broadly, we respectfully suggest that the Proposal also does not fully address the FDIC's stated concerns and unfortunately creates new challenges for the FDIC and for financial institutions. As we discuss in this letter, the Proposal fails to address fully potential public confidence issues, could impair efficient administration of a receivership, may lead to customer confusion, could undermine international cooperation, and could present risks to the FDIC's resolution of an international banking institution with resulting consequences for the Deposit Insurance Fund (the DIF). Furthermore, the Proposal poses operational, regulatory, and competitive risks to banking institutions that can be avoided if the Proposal were modified so as also to include the interpretation of "deposit liabilities" that we discuss in this letter.

We believe that the most effective way of addressing all of the concerns of the FDIC and the industry, while also directly resolving both the international depositor preference issue and the FDIC's concern about becoming "insurer to the world," would be to adopt an approach that combines the deposit insurance determination in the Proposal with a determination that foreign deposits are "deposit liabilities" for purposes of Section 11(d)(11) of the Federal Deposit Insurance Act (the FDIA).

If the depositor preference issue is addressed by adopting this determination that would eliminate subordination of foreign depositors and the key incentive to adopt dual pay would be removed, thereby solving the FDIC's concern about expanding insurance coverage. However, the converse is not true – if the *insured status* of foreign deposits is merely clarified, the international friction spurred by the differential treatment in liquidation of foreign deposits remains unresolved.

We recognize that undertaking this more direct and complete approach may require either or both a new proposal (in order to provide appropriate notice and opportunity for comment for new aspects of the proposal) or a reinterpretation of prior informal positions. Neither of these presents an insurmountable challenge or delay, yet there would be immense benefits from legal certainty and clearly avoiding all of the issues and costs described in this letter. We urge the FDIC to take this course.

In this letter we discuss key issues that were not addressed or fully considered in the Proposal and make the following points:

- The Proposal focuses solely on a narrow method of containing the amount of insured deposits without addressing the depositor preference issues, without adequately assessing the unintended consequences of the Proposal, and without considering the more optimal combined approach described above.

⁸ See footnote 44 below and its accompanying text.

- The combined approach would, in fact, address all of the underlying factors that led to the current Proposal as well as mitigate the negative consequences and costs of implementing the Proposal alone.
- The Proposal appears based, in part, on an overestimation of the desire of the industry to enter into dually payable deposit structures and of the speed with which the industry may implement such measures, while underestimating the costs and other unintended consequences of forcing banks to adopt dually payable deposits to resolve the depositor preference issue. Dual payability is not the best approach and should be seen as an option only by comparison to much more troubling options from the point of view of bank customers, banks, and the regulatory agencies involved.
- The Proposal creates new challenges and risks, adds complexity to the FDIC's role as conservator or receiver, and impedes the efficient resolution of cross-border institutions. In any future resolution of a cross-border U.S. bank, there is a very strong likelihood that the FDIC will be sued to challenge the denial of deposit insurance coverage for dually payable deposits. In addition, any solution that depends exclusively on deposit contracts, coupled with the likely diverging requirements in multiple host jurisdictions, will lead to a need for FDIC interpretations, the potential for significant uncertainty, and inevitable differences in protection from jurisdiction to jurisdiction, in any future failure. These risks were not discussed in the Proposal.
- There are significant risks to the industry, and to banking customers, if the Proposal is adopted in its current form without other action by the FDIC. These include negative consequences to liquidity, contractual complexity, customer confusion and uncertainty, international regulatory uncertainty, potential need for multiple and varied approaches to resolve the depositor preference issue, need for regulatory opinions to answer questions not addressed in the Proposal, increased costs, and increased regulatory burdens. Such impacts would affect any bank – large or small – that has or wishes to establish a branch in another country. These harmful effects would all be avoided under the combined approach described above and therefore would be unnecessary costs and burdens that would negatively impact the provision of financial services to the economy.

We appreciate the opportunity to submit this comment letter and would appreciate further opportunities to discuss the advantages of a comprehensive solution to the depositor preference and deposit insurance issues that are the source of concern and friction for all U.S. banks that operate deposit-taking branches internationally. Our members are also willing to meet with the FDIC to explain the challenges and costs that a dual payability regime would impose on bank customers, banks, regulatory resolution mechanisms, and the economy.

II. Background – A Different Solution Would Address All of the Underlying Factors that Led to the Current Proposal and Would Benefit the FDIC

The issues surrounding the treatment of deposits at foreign branches of U.S. banks and of depositor preference are not new. As the Proposal notes, the FDIC was created in 1933 to offer a

backstop to depositor risk. Language excluding deposits at foreign branches from total insured deposits or from the definition of “deposits” also originates from that time period.⁹

Indeed, it was this long-standing language¹⁰ that created confusion about the status of foreign deposits when depositor preference was added to the FDIA in 1993.¹¹ Under depositor preference, “deposit liabilities” receive preference over general unsecured creditors in the liquidation of an insured depository institution.¹² Observers have noted that the primary reason for enacting the depositor preference provisions was to assist the government in meeting budgetary constraints,¹³ as the FDIC would thereby, in subrogation of the claims of those holding deposit liabilities, rank ahead of other creditors. However, depositor preference raised a new issue. With the *already existing* exclusion of deposit liabilities at foreign branches of U.S. banks from the meaning of “deposit” under the FDIA, the adoption of depositor preference raised a question as to whether foreign depositors would or would not be covered by the preference. There was no specific evidence that Congress intended to exclude foreign deposit liabilities from depositor preference.

The then-Acting General Counsel of the FDIC briefly addressed the question in an Advisory Opinion in 1994.¹⁴ The 1994 Advisory Opinion concludes, with limited discussion of the potential issues, that “‘deposit liability’ under the National Depositor Preference statute does not include obligations payable *solely* at a foreign branch or branches of a United States chartered bank” (emphasis in original). The 1994 Advisory Opinion arrives at this conclusion notwithstanding the lack of evidence that Congress intended this outcome.¹⁵

The interpretation of the 1994 Advisory Opinion has created substantial friction in international discussions concerning the resolution of internationally active banks throughout the

⁹ See 12 U.S.C. § 264 (1933) (excluding from deposit insurance “amounts of all deposits of such bank which are payable only at an office thereof located in a foreign country”); 12 U.S.C. § 264(c) (1935) (excluding from the definition of deposit “any obligation of a bank which is payable only at an office of the bank located outside the” United States).

¹⁰ The definition of “deposit” is now in 12 U.S.C. § 1813(l) and the exclusion from the definition for deposits at offices “located outside of any State” (subject to exceptions) is now in 12 U.S.C. § 1813(l)(5)(A).

¹¹ See Omnibus Budget Reconciliation Act of 1993, Pub. Law 103-66, 107 Stat. 312 (1993).

¹² See 12 U.S.C. § 1821(d)(11).

¹³ See James A. Marino and Rosalind L. Bennett, “The Consequences of National Depositor Preference,” FDIC Banking Review 12, no. 2, at 22. (Oct. 1999) (hereinafter, Marino & Bennett) (“The main impetus behind passage was that it allowed Congress to project cost savings to the FDIC and use those projected savings to offset part of the projected U.S. budget deficit.”)

¹⁴ “‘Deposit Liability’ for Purposes of National Depositor Preference Includes Only Deposits Payable in U.S.,” FDIC Advisory Opinion 94-1 (Feb. 28, 1994) (the 1994 Advisory Opinion).

¹⁵ We mention this issue of congressional intent because without legislative intent to exclude foreign deposit liabilities it should be significantly easier to address directly the issue of subordination of foreign depositors with an interpretation that they do benefit from depositor preference, rather than attempting to effect a solution to the depositor preference issue indirectly through an interpretation of the insured status of dually payable deposits.

ensuing years. Foreign regulators have consistently expressed concern and displeasure that depositors in the branches of U.S. banks within their borders would be subordinated to depositors in branches (of the same bank) located in the U.S. This has consistently been an obstacle to improved coordination and an incentive to ring-fencing if a U.S. bank with international operations were placed into FDIC receivership.¹⁶

Yet up to the current time customers in general have not required, and as described in both the Proposal and this letter, banks have not typically offered, “dual payability” of deposits in a U.S. branch as a solution to these concerns. Generally, there has been no real interest by customers in receiving dually payable deposits. Moreover, U.S. banks have historically *resisted* providing dually payable deposits in the very rare occasions when a client has made such a request. While U.S. banks have had the opportunity for 20 years unilaterally to adopt dual payability for the benefit of their foreign depositors, they have not done so because of the potential additional consequences (described throughout this letter) that such adoption would entail. The FDIC specifically recognizes that, despite a significant increase in foreign branch deposits since 2001, “the overwhelming majority of the deposits in . . . foreign branches of the United States banks are payable only outside the United States.”¹⁷ There simply has been no significant market reason for U.S. banks to institute dual payability for foreign depositors, and, in fact, significant reason not to do so.

While the issue had long existed, the necessity for a solution became evident when the UK FSA issued a Consultation Paper in September 2012.¹⁸ The FSA Consultation Paper proposed that non-U.K. and non-European Economic Area banks organized in a jurisdiction with a depositor preference regime that favors domestic deposits be prohibited from accepting deposits in the U.K. unless the subordination of U.K. depositors is rectified in some manner.¹⁹ The UK FSA originally expected to issue final rules by January 2013 and expected banks to make relevant disclosures by April 2013. The FSA Consultation Paper has essentially forced U.S. banks to seek change to what has been the *status quo*.

In this context, our members began exploring (including in meetings with the FDIC) potential ways to avoid the drastic consequences of having branch operations in the UK, and potentially in other nations, shuttered. Initially, we and our member banks were primarily concerned with developing solutions fully within our control. One potential avenue is

¹⁶ See, e.g., Financial Stability Board, “Key Attributes of Effective Resolution Regimes for Financial Institutions,” (Oct. 2011) ([FSB Key Attributes](#)) at Key Attributes 7.4 and 7.5 (“National laws and regulations should not discriminate against creditors on the basis of their nationality, the location of their claim or the jurisdiction where it is payable. . . . Recognition or support of foreign measures should be provisional on the equitable treatment of creditors in the foreign resolution proceeding.”)

¹⁷ 78 Fed. Reg. at 11,605. See also 78 Fed. Reg. at 11,607 (“Historically, the great majority of deposit agreements governing relationships between United States banks and their foreign branch depositors have not expressly provided for payment of foreign branch deposits at an office in the United States”).

¹⁸ UK FSA, “Addressing the implications of non-EEA national depositor preference regimes,” Consultation Paper CP 12/23 (September 2012) (the [FSA Consultation Paper](#)).

¹⁹ See FSA Consultation Paper at §§ 1.9 and 3.4.

implementing a dually payable deposit structure in the U.K. and the U.S. Yet, the FDIC should not misconstrue the *availability* of this option for *desirability* of this option. Another option, “subsidiarization,” is even more objectionable, however. Both are superior to shutting down operations in the U.K. (and in other nations that follow the U.K.’s lead), while dual pay seems less harmful than incurring the detrimental capital, resource, and resolution inefficiencies of subsidiarization of U.K. branches of U.S. banks.

Given the clear negative consequences of subsidiarization, dual pay remained as the only viable option within the control of the banks themselves. However, adopting dually payable deposits has never been the preferred option. The preferred option is a regulatory solution that eliminates the subordination of foreign branch depositors without requiring dual payability of those deposits. We are confident that U.S. banks would not adopt dual payability unless there were no better alternative available to comply with the proposed U.K. requirements.

Complementing the banks’ discussions with the FDIC, three U.S. law firms (Cleary Gottlieb Steen & Hamilton LLP, Davis Polk & Wardwell LLP, and Sullivan & Cromwell LLP) provided the FDIC with a memorandum on January 2, 2013, that proposed a solution through regulatory rulemaking or interpretive guidance. The memorandum provided clear legal and policy support for a regulatory interpretation of the term “deposit liabilities” in FDIA § 11(d)(11) as including deposits at foreign branches of U.S. banks.²⁰ Such an interpretation would afford deposit liabilities in foreign branches the benefit of depositor preference, would avoid such deposit liabilities becoming “deposits” for purposes of FDIC insurance, and would not require U.S. banks with foreign branches to adopt dually payable deposits and thereby restructure client relationships in ways that neither bank nor customer wants.

On February 4, 2013, the three law firms submitted a supplement to that memo indicating that the combination of (a) an interpretation of “deposit liabilities” as including foreign branch deposits *and* (b) a regulatory determination that dually payable foreign branch deposits were not insured, could be an alternative that addressed a broader set of concerns and would be far superior to an interpretation that *only* involved eliminating insurance for dually payable deposits.²¹ This is the combined approach we advocate.

The purpose of this combined approach is to provide a *direct* solution to the FSA Consultation Paper and to the problems confronting the industry and the FDIC. The conclusion of the 1994 Advisory Opinion may have been only an irritant previously. Today, the subordination of foreign deposits risks impairing international coordination and imposing significant consequences on the FDIC and U.S. financial institutions. The FSA Consultation Paper makes this clear, and we can expect similar approaches by other regulators, although the varying approaches they may take to the problem risks fostering uncertainty.

²⁰ Cleary Gottlieb Steen & Hamilton, Davis Polk & Wardwell, and Sullivan & Cromwell, “The Status of Foreign Branch Deposits Under the Depositor Preference Rule” (Jan. 2, 2013). A copy of this memorandum is included in [Appendix A](#) to this letter.

²¹ Cleary Gottlieb Steen & Hamilton, Davis Polk & Wardwell and Sullivan & Cromwell, “Status of Foreign Branch Deposits: Alternative Approach” (Feb. 4, 2013). A copy of this supplement is included in [Appendix B](#) to this letter.

A solution *requires addressing both* the deposit insurance *and* depositor preference issues by a regulation, or other final and binding statement by the FDIC; only that combined approach fully and completely addresses these issues as a matter of law. Adopting this approach and updating the conclusion in the 1994 Advisory Opinion to reflect the changes in international regulatory and resolution coordination, within the context of the statute and the needs of policy, would, in one simple yet comprehensive solution, address directly all of the concerns with the *status quo* recognized by the FDIC, foreign regulators, and the industry, and in the most optimal way for bank customers. It is important to recognize that the 1994 Advisory Opinion, however justified at the time, was not adopted by the FDIC board of directors as a formal opinion, nor was it ever incorporated into legislation or regulation. Therefore, the FDIC should not be constrained by that decision nor prevented from developing a formal updated interpretation and regulation that will provide legal certainty to banks, depositors, and foreign regulators in accordance with evolved international conditions.

In addition to all of the arguments in the initial and the supplemental memoranda from the law firms, we submit that as a practical matter it should not be a challenge to recognize that a “deposit” and a “deposit liability” are the same from a balance sheet perspective, if not from a deposit insurance perspective. Therefore, a “deposit liability” from a balance sheet perspective would include all deposits, whether domestic or foreign. The difference surfaces only when analyzing the statutory definition and usage of these terms – the common balance sheet understanding of “deposit” was changed in FDIA § 3(1)(5) simply to narrow deposit insurance coverage and exclude those deposits payable overseas. No similar change was made to the common understanding of “deposit liability” in the statute. As a result, for purposes of the statute, where “deposits” are relevant, the more narrow definition can and should be used. However, in the context of depositor preference, the common understanding of “deposit liability” as including all deposits on a balance sheet is more consistent with the balance sheet treatment for those liabilities.

The depositor preference statute concerns the payment of bank creditors and is therefore focused on balance sheet concepts of using assets to address liabilities. The statute creates a hierarchy of creditor claims for the payment of *all* of the liabilities on a balance sheet. As a result, depositor preference is not intended to incorporate all of the policy considerations underlying the definition of “deposit” for deposit insurance and related provisions. The distinctions between a “deposit liability” and “deposits” provide a reasoned approach to different statutory terms and the FDIC has ample authority to adopt this approach in relation to the resolution and liquidation of banks.²²

We strongly believe that the FDIC should take this opportunity and supplement the current Proposal with an additional interpretation including foreign deposits in the meaning of “deposit liabilities” under FDIA § 11(d)(11). The key benefit of adopting this approach is simple – it would avoid all of the negative consequences that we raise in this letter. In addition, the combined approach would yield significant benefits for the FDIC:

²² See FDIA § 11(d)(1).

- Unlike the current Proposal, it would, in fact, address every one of the four concerns that the FDIC noted in the Proposal – maintaining public confidence, protecting the DIF, ensuring an effective and fair resolution of a troubled institution, and enhancing international cooperation.
- By addressing the depositor preference issue directly, it would remove the need for banks to adopt dually payable deposits and therefore would reduce the risks of uncertainties from potential litigation over the current Proposal. By incorporating the proposed regulation, the approach would protect the FDIC from becoming “insurer to the world” for dually payable deposits that may in the future be adopted for other reasons.
- It would bolster international cooperation, rather than exacerbate international tensions. The international regulatory community would appreciate the direct and comprehensive nature of the solution, in contrast to the possible patchwork application of dual payability that banks would otherwise be compelled to adopt. Foreign regulators would recognize that the current Proposal does nothing for the subordination of their depositors without some action by the banks.
- This combined approach would, in one simple move, make U.S. regulation compatible with the FSB Key Attributes and the EU Resolution and Recovery Directive.
- The combined approach would entirely eliminate a whole new set of potential risks and potential costs for the FDIC. The current Proposal invites significant ambiguities, and it is inevitable that U.S. banks, foreign depositors, and foreign regulators will have an ongoing need for guidance on the various permutations of dual payability and its efficacy under both U.S. depositor preference and foreign rules attempting to elevate the status of their local depositors.
- Dual payability would also have significant regulatory reporting and international monitoring costs that the FDIC can avoid through adoption of the combined approach.
- The recommended combined approach would preserve the FDIC’s determination that foreign deposits (even those that are dually payable) do not benefit from deposit insurance, and it therefore would address the FDIC’s concern about prompt payment to insured depositors. At the same time, it would not raise additional complications in resolution that would arise under dual payability, such as confusion over where and whether payment on deposits were made, regulatory arbitrage caused by providing depositors with multiple options for the location of their claim, the possibility of hampering purchase and assumption transactions while purchasing entities sort out where a deposit is to be housed, and increased complexity of related legal proceedings.
- The FDIC would be promoting the safety and soundness of the industry. Costs of implementing dual payability would be avoided, and the possibility of procyclical

impacts on stressed institutions from the additional withdrawal opportunities afforded to depositors would be negated.

We appreciate the FDIC's willingness to set the rulemaking machinery in motion to respond to this international conundrum. Further, we fully agree with an approach that does not make the FDIC "insurer to the world." The Proposal, however, adopts only the insured deposit interpretation which, in our view, is inadequate. It is inferior to both the recommended updated deposit liability interpretation alone and also to the combination of the FDIC Proposal and the updated interpretation. Indeed, inclusion of the deposit liability interpretation is necessary to address *finally and conclusively* the subordination of foreign depositors while eliminating any incentive for depositors and host regulators to require, and banks to feel compelled to offer, dually payable deposits.

III. There is Sufficient Time to Adopt a Combined Approach, as Implementation of Dually Payable Deposits is Not Imminent

The Proposal expresses a significant concern about the imminence of a unilateral adoption of dually payable deposits by the industry and therefore a related apprehension about potential impact on the DIF if the deposit insurance status of dually payable foreign deposits is not clarified.²³ Although we appreciate the speed with which the FDIC has already acted, we believe that there is time to come to a more complete response to all of the concerns arising from this challenge and the issues related to insurance for foreign deposits.

As noted above, dual payability is the only option open to the industry, aside from subsidiarization, if there is no legislative or regulatory solution. We appreciate the early opportunities afforded to ABASA and its members to meet with the FDIC to discuss the FSA Consultation Paper and its ramifications, well before any regulatory rulemaking process had begun. During those meetings, the banks informed the FDIC that dually payable deposits are not a desirable solution and that a legislative or regulatory solution is preferred. The banks did indicate that dually payable deposits *could* be implemented if there were no other legislative, regulatory, or internationally negotiated solution available in response to the timing pressure initially received from the UK FSA. Short of subsidiarization, which is not favored by the industry at all, there is no other solution that the banks can effect themselves. Thus, the fact that the banks raised the dual pay option should have been no surprise, but it was clearly stated not to be a desirable solution.

However, changes have occurred since the time that the banks met with the FDIC. First, in early December 2012, the UK FSA extended the comment period on the FSA Consultation

²³ For example, the FDIC notes that dual payability is an imminent "threat" to the DIF and that "absent decisive action, the FDIC could find itself subject to liability to depositors throughout the world." 78 Fed. Reg. at 11,607 and 11,605. There are several other statements that we believe exaggerate the imminence of any impact on the DIF. *See also* 78 Fed. Reg. at 11, 605-6 ("United States banks have advised the FDIC that they are likely to begin the process of sending out these disclosures shortly and, further, that they would likely make their deposits payable both in the United Kingdom and the United States at the same time or shortly thereafter to minimize the likelihood of deposit run-off and mitigate any potential damage to their customer relationships. . . . Absent timely direction from the FDIC, there could be significant impact on the FDIC's deposit insurance program"); 78 Fed. Reg. at 11,607 ("This threat is aggravated . . .").

Paper and has since expressed willingness to engage in further discussion about the timing of disclosures and implementation of solutions to the FSA Consultation Paper. Second, the FDIC has, in fact, commenced a rule writing process, thus providing an opportunity to create a clear and direct solution to the issue that does not require the banks to work with the very limited tools that they can wield solely by themselves.

As a result, there is time and opportunity to consider the full range of issues raised by the FSA Consultation Paper and the FDIC Proposal so that the optimal solution can be adopted. We recognize that the combined option that we discuss in this letter, and that was more fully described in the law firm memo and supplement, may require a revised proposal (or “reproposal”) as well as updating the 1994 Advisory Opinion. The FDIC Proposal itself requires a modification of the approach in the 1994 Advisory Opinion because the Proposal precludes deposit insurance for dually payable deposits even though the 1994 Advisory Opinion concluded that deposits payable within the U.S. are “deposits” for purposes of the FDIA. Now that the FDIC, the U.S. banking industry, and the U.K. regulators all are actively contemplating solutions to these issues, we recommend that the FDIC address the underlying concern rather than solely the issue of insurance coverage for dually payable deposits.

IV. The Proposal Presents Risks to the FDIC’s Role as Receiver, and to the Efficient Resolution of Cross-Border Institutions

Dual payability would present additional issues for the FDIC and financial institutions that can be avoided by the approach we recommend. While the intent of the Proposal is to avoid potential liability to the DIF “that could be global in scope”,²⁴ relying on dual payability also threatens to expose the DIF to risks and would introduce more complications into the resolution of international institutions.

A. The Proposal Complicates Orderly Resolution of U.S. Banks with International Operations and Exacerbates Stress Situations for Such Banks

The Proposal threatens to complicate bank resolutions. In a resolution, the FDIC and the host jurisdiction are likely to experience increased logistical risks, increased need for coordination and cooperation, multiple claims from the same depositor, and legal proceedings aimed at determining which depositors have been paid. There are inherent complications to the necessary record-keeping for deposits that are payable in two jurisdictions that will require continued review by banks, by the FDIC, and by different host jurisdictions. Like the complications involved in preventing double payment of deposit insurance for dually payable deposits in the absence of the Proposal, there will be complications in coordinating the resolution and management of branches with deposits that may be withdrawn in two jurisdictions. In addition, there is the potential for inconsistent treatment and potential double payment if a U.S. bank’s overseas branch is ring-fenced for resolution. These risks were not evaluated in the Proposal and demand careful consideration if the Proposal were to be adopted unamended.

²⁴ 78 Fed. Reg. at 11,607.

Another issue presented by a dual pay regime that requires careful consideration is the potential financial stress caused by deposit withdrawals and deposit flows. As we have amply seen in recent decades, the demand for U.S. dollars rises in times of either localized or general international financial stress.²⁵ Foreign depositors with dual pay accounts would have greater opportunity and flexibility to make withdrawals,²⁶ and could forego deposit withdrawals in their local currency (or circumvent prohibitions on withdrawals of local currency²⁷) to access U.S. dollars through a U.S. office. As discussed below, U.S. banks are likely to limit withdrawals from a U.S. office to U.S. dollars. While this condition will restrict somewhat the flexibility of foreign depositors, it ironically will provide a direct line for the withdrawal of U.S. dollars from U.S. banks – a capability not previously available to foreign depositors outside of account-specific contracts to permit multiple currency withdrawal. The additional venues for withdrawal and the new accessibility to U.S. dollars exposes an internationally active U.S. insured depository institution to unexpected withdrawals and potential runs in instances of foreign instability and uncertainty – precisely when the bank needs to maintain market confidence and a strong asset base.

At an aggregate level, the sudden demand for large volume withdrawals of U.S. dollars under an international stress scenario also would introduce a procyclical variable when global bank supervisors are making efforts to bolster liquidity and increase the safety and soundness of banking institutions. The incentive and opportunity for large withdrawals as outlined above would have the effect of pushing stressed banks deeper and quicker into crisis scenarios, exacerbating economic uncertainty, and lending credence to customer fears about bank instability. As a result, dual payability and the multiple avenues for depositors to withdraw funds increases the threat of a bank run and expands the universe of operational uncertainties for the bank and its U.S. and foreign host regulators, while intensifying the monitoring burden for liquidity stress.

Moreover, because foreign depositors remain uninsured under the Proposal,²⁸ they are motivated to withdraw in times of market stress.²⁹ Indeed, the FDIC stated in its Final Rule on

²⁵ See, e.g., Robin Harding, “Nervous Europe drives demand for dollars,” *Financial Times*, Apr. 7, 2013.

²⁶ See Marino & Bennett at 36-37 (“Uninsured depositors and unsecured creditors . . . will protect their interests more actively and thus precipitate a liquidity failure much more rapidly . . .”). Foreign depositors will make this choice to withdraw from a U.S. branch for a number of reasons, including the desire for U.S. dollars and the potential desire to skirt host country restrictions on deposits. To be clear, we are not suggesting that all depositors would do so, but are highlighting the increased opportunity granted to depositors that will inevitably lead to likelihood of use of that opportunity – an opportunity attendant with liquidity and related risks that would be unnecessary to incur under the combined approach.

²⁷ In providing a source of withdrawals from outside the foreign host jurisdiction, dual pay will encourage depositors to *evade host-imposed limits* on withdrawals. For example, a host jurisdiction may limit withdrawals in market stress scenarios, but dually payable accounts provide an avenue for runs out of U.S. offices that was not previously available. Thus, forcing dual payability will expose U.S. offices to the risk of runs due to foreign instability, weaken U.S. institutions at the expense of domestic depositors and increase the likelihood of failure. The letter addresses further the issue of sovereign risk in Section V.C. below.

²⁸ Unless otherwise covered by a host country deposit insurance regime, which is currently rare.

large bank assessment pricing that foreign depositors are more likely to withdraw than domestic depositors, and it reflected this belief in its assessments guidelines.³⁰ In addition to the greater probability of runs and, by extension, bank stress, dual payability also would *increase losses* to the DIF in the event of a bank failure were the host regulator to ringfence local bank assets. As explained above, increased withdrawals from foreign depositors may pull assets and liquidity from the U.S. parent bank. The ringfencing order of the host regulator would trap assets in the host country and make funds unavailable for covering U.S. insured deposits at time of resolution.³¹ Also, because dual pay will increase the speed with which a bank may become unstable due to potentially higher volumes of sudden draws on liquidity, the FDIC will have less time to identify, intervene, and facilitate an orderly resolution of a U.S. bank with international operations.

B. The Proposal Invites Uncertainty and Litigation in an FDIC Resolution of a U.S. Bank with International Operations

The Proposal invites foreign depositors to sue the FDIC, during a bank resolution, to claim that they should be insured under FDIA §§ 3(l)(5)(A) and 3(m). As highlighted in the law firm memo, we believe that interpreting “deposit liabilities” to include foreign deposits for purposes of FDIA § 11(d)(11) will eliminate the risk of litigation over depositor preference, as well as virtually eliminate the risk of litigation by foreign depositors over deposit insurance, because there will be few dually payable deposits.

As revealed in the Proposal and conversations with the FDIC, there is a possible misapprehension that industry believes that litigation following a future failure is *unlikely*. In contrast, ABA and ABASA specifically believe that the Proposal increases the likelihood of

²⁹ Even with dual pay potentially correcting the subordination of foreign depositors, foreign depositors are more apt than U.S. depositors to seek withdrawal from any source they can, particularly if they remain uninsured. *See Marino & Bennett at 27* (in studying several bank failures before the 1993 institution of depositor preference and its disadvantages for foreign depositors, it was “clear that a troubled bank’s liability structure changes considerably as it approaches failure. In all of [the cases reviewed in the article,] total liabilities decreased, uninsured and unsecured liabilities fell relative to insured deposits, and foreign deposits declined.”); *id.* at 35-36 (finding that “Exposed creditors might be more skittish and therefore more prone to run or seek collateral. Uninsured depositors and unsecured creditors might move more aggressively to protect themselves” and “uninsured depositors and unsecured creditors of troubled banking institutions always seek to protect themselves. At failure, the amount of uninsured deposits and unsecured liabilities is much less than it was in the months or years before failure”).

³⁰ FDIC, “Assessments, Large Bank Pricing,” 76 Fed. Reg 10,672, 10,695 (Feb. 25, 2011).

³¹ This possibility was also noted by the FDIC in the Final Rule on large bank assessments. 76 Fed. Reg. at 10,695. The FDIC and Federal Reserve have also recently released guidance in relation to resolution planning, requesting that banks address as an obstacle to resolution the risk that foreign regulators’ actions following a resolution “could result in ring-fencing of assets or lead to other outcomes that could exacerbate financial instability in the United States.” *See* FDIC and Federal Reserve, “Guidance for 2013 § 165(d) Annual Resolution Plan Submissions by Domestic Covered Companies that Submitted Initial Resolution Plans in 2012” (April 15, 2013) at Section II.A.2 and at Attachment A.1.d. and D.2. Indeed, we submit that adoption of the combined approach we advocate would be a “potential mitigant by which [a bank] might lessen the likelihood that regulators in the jurisdiction housing a funding hub might restrict the transfer of liquidity out of that jurisdiction.” *See id.* at Attachment D.2.b.

dually payable deposits and hence the likelihood of litigation. Furthermore, the Proposal is likely to increase the related uncertainty surrounding claims against branch assets. If dual payability is the only remaining acceptable option for eliminating subordination of foreign depositors, and as a result the number of dually payable deposits increases dramatically, it is to be expected that depositors will have every incentive to seek insurance coverage from the DIF and challenge the Proposal in court.³² Litigation risk is further aggravated by the likelihood of claims across jurisdictions, potentially under different resolution regimes, thus increasing the complexity of resolution, increasing the cost to the DIF, and delaying the fulfillment of claims by the FDIC.³³

With dual payability, there is a greater likelihood of customer confusion. Disclosure becomes more complex and confusion more likely for less sophisticated retail customers.³⁴ Even large multinational corporate depositors are unlikely to understand all the implications of dually payable deposits, which will be exacerbated if business customers use branches of the same bank in dual pay and non-dual pay geographies.³⁵ This confusion may also increase the likelihood of litigation against a U.S. institution itself.

C. The Recommended Approach Would Reinforce FDIC’s Role in Promoting International Coordination and Cooperation

The FDIC has consistently sought to achieve greater international cooperation in the wake of the financial crisis both to facilitate its traditional role of deposit insurer and receiver for insured banks and to implement its expanded responsibilities under the Dodd-Frank Act. Given the long-standing criticisms by multinational organizations and by national regulators of the subordination of foreign depositors under the 1994 Advisory Opinion, FDIC action to eliminate the potential for such subordination by interpreting “deposit liability” to include foreign depositors will more effectively achieve these important goals. Due to the potential for inconsistent actions by host jurisdictions and a multiplicity of dual payability requirements in those jurisdictions, there is the substantial likelihood of disparate and inconsistent approaches. A uniform interpretation by the FDIC is the most effective way to achieve the goal of eliminating

³² See Marino & Bennett at 36 (“uninsured depositors and unsecured creditors of troubled banking institutions always seek to protect themselves”).

³³ See Marino & Bennett at 26 (“The process of determining insurance requires detailed analysis of bank liabilities to determine those that are uninsured and unsecured. It is therefore extremely labor intensive and expensive, especially for a large bank.”).

³⁴ Another consequence of the Proposal is that explanatory disclosure becomes much more difficult. Under an interpretation that includes foreign deposits in “deposit liabilities” under FDIA § 11(d)(11), disclosure is simple and understandable – deposits now receive the benefit of depositor preference in a liquidation of a U.S. institution. Under the Proposal, U.S. banks will be required to inform depositors that they *do not* benefit from depositor preference, unless they enter into a dually payable deposit contract. Disclosure may also require a discussion of “how” the dually payable deposit provides this benefit, whether the local regulators believe that dual pay is acceptable and is in compliance with any local regulatory requirements to eliminate subordination of depositors, and other matters (such as those described in section V.C. below that limit the obligation to pay in a U.S. office).

³⁵ As mentioned below, our member banks are not likely to offer dual pay flexibility in jurisdictions where it is not otherwise required to address foreign depositor subordination or similar issues.

the impediment to cooperation represented by foreign depositor subordination. Despite the preamble's stated support for international cooperation, U.S. policy after the Proposal still would be inconsistent with agreed international principles of a global resolution regime, as the interpretation in the Proposal on deposit insurance does not, in fact, address depositor preference.³⁶

As noted above, the effect of implementing the Proposal unchanged would be to drive the industry to make deposits dually payable for U.K. depositors in order to comply with the proposals in the FSA Consultation Paper. Since, however, dual pay presents all of the risks to the banks discussed in this letter, our members believe that they and other banks will limit the application of dual payability to depositors in those jurisdictions, such as the U.K., that raise the issue. Thus, a significant number of foreign depositors in various jurisdictions will still be subordinated to U.S. depositors. At the same time, this approach will likely raise the ire and frustration of foreign regulators as they realize they will have to follow the UK FSA example, which may lead to the spread of dual payability in a piecemeal fashion over time. This evolution will be costly, inefficient, and contribute to uncertainty as the status of depositor subordination and of dual payability from jurisdiction to jurisdiction remains in flux. Further, divergent requirements in different host jurisdictions will lead to uncertainty and potential lack of cross-border coordination, as well as significant regulatory risk for banks. These staggered and inconsistent developments will lead to further required monitoring by the FDIC of these different approaches, with further incurrence of costs for such monitoring, as well as the need for the FDIC to respond, on a continuous and ongoing basis, to questions about the implementation of dually payable deposits and the efficacy of this approach in addressing depositor subordination issues.

In its most recent draft of April 15, 2013, Article 86.1(c) of the draft EU Resolution and Recovery Directive (RRD) allows European authorities to refuse to recognize or enforce third country resolution proceedings, if the authority found "that creditors, including in particular depositors located or payable in a Member State, would not receive equal treatment with third country creditors and depositors under the third country resolution proceedings".³⁷ While the RRD remains in development, it is likely that a final version will include some version of this authority, consistent with the FSB's Key Attributes, to refuse to recognize or enforce insolvency proceedings that may discriminate against depositors.³⁸ This would undermine the Dodd-Frank

³⁶ See FSB Key Attribute 7.4 ("National laws and regulations should not discriminate against creditors on the basis of their nationality, the location of their claim or the jurisdiction where it is payable.")

³⁷ See Proposal for a Directive of the European Parliament and of the Council establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directives 77/91/EEC and 82/891/EC, Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC and 2011/35/EC and Regulation (EU) No 1093/2010 – Presidency compromise, Interinstitutional File: 2012/0150 (COD) (Apr. 15, 2013), Article 86.1(c).

³⁸ A recent FSB Report, in its analysis of factors relevant to cross-border cooperation and resolution, notes that the U.S. is one of only eight jurisdictions that provide for differential treatment of creditors (including depositors and policyholders) by location of their claim or the jurisdiction in which the claim is payable, and that the vast majority of jurisdictions do not discriminate in this manner. The other seven jurisdictions are: Australia, Indonesia, Japan, Korea, Singapore, Switzerland, and Turkey. These eight countries, including the U.S., are therefore the exception to the international consensus to refrain from such discrimination against depositors, which

Title II orderly resolution effort, and, *a fortiori*, the single point of entry resolution model advocated by the FDIC.

The FDIC has the opportunity to adopt an interpretation that would bring regulatory certainty to international regulators and depositors, eliminate the incentive for a piecemeal application of dual payability by banks, avoid the frustration and inevitable patchwork of foreign jurisdictions that might otherwise insist on a resolution of the depositor preference issue for their home country depositors, and resolve the inconsistency of the U.S. depositor preference regime with internationally agreed standards.

D. The Proposal Requires Further Explanation by the FDIC of Alternatives (or Rejected Alternatives) in Order to Be Consistent with Administrative Procedure

We believe that the Proposal should have more fully addressed alternatives, including addressing in more detail the possible updating of the 1994 Advisory Opinion and the proposals in the law firm memo and supplement. Further discussion of alternatives would have provided a more complete record for comment. As a matter of administrative procedure, alternatives should be discussed in order to provide appropriate opportunity for comment by all interested parties on the entirety of the Proposal.

V. Risks to the Industry, and Significant Questions that Arise, if the Proposal Is Adopted in its Current Form

In the Proposal, the FDIC identifies only two costs of undertaking dual pay deposits – the possibility that the deposits would attract additional insurance assessments and the fact that the deposits would be subject to reserve requirements under Regulation D, as promulgated by the Board of Governors of the Federal Reserve System (the Federal Reserve).³⁹ The FDIC failed to discuss additional risks to both the industry and the FDIC of effectively forcing dual pay as a solution to the international depositor preference issues.

We wish to emphasize that the costs, challenges and inefficiencies we discuss below are not merely about the *potential* impacts to business from future litigation, customer confusion, or resolution of a financial institution – many, if not all, of the issues we discuss below directly affect how banks will do business and address client concerns today.

A. Banks Are also Negatively Affected by the Risks to the FDIC and to the DIF Described Above

Many of the risks to the FDIC discussed above also are of great concern to the industry, because embedded in each of those FDIC issues are also risks to the safety and soundness of the industry, with significant uncertainty as to how international regulatory issues around depositor preference will ultimately be concluded.

could impede efforts by these eight countries to promote cross-border cooperation in resolution. *See* Financial Stability Board, “Thematic Review on Resolution Regimes – Peer Review Report” (Apr. 11, 2013).

³⁹ 12 C.F.R. Part 204. The FDIC also notes a “concern” by the industry of losing protection from sovereign risk accorded to banks under 12 U.S.C. § 633; we discuss this further below.

First, the greater probability of runs and bank stress due to potential claims on the U.S. home office from foreign depositors is of great concern to the industry. This liquidity uncertainty may only worsen over time if more jurisdictions follow the example of the UK FSA and the FDIC has failed to take steps that protect banks from being forced to adopt dual payability. Similarly, the need under dual pay to maintain higher liquidity amounts in both U.S. and non-U.S. offices (and in the local currencies of each office)⁴⁰ subjects banks to unnecessary opportunity costs related to the potential alternative uses of that liquidity.⁴¹ The liquidity effect during normal operations is real – we understand that, for a deposit solely payable outside the United States, a foreign depositor could currently withdraw its deposit and re-deposit the amounts in the United States. Unlike a dual payability structure, however, this would reduce foreign branch assets and liabilities, reduce the need for liquidity to be maintained in both places, and would reduce assets and liabilities caught in a potential foreign ring-fence.

Second, the FDIC Proposal increases the possibility that a foreign jurisdiction could choose to address the depositor preference issue—since the Proposal does not resolve that issue—by requiring subsidiarization, particularly if the jurisdiction rejected dual pay as an option. Subsidiarization imposes significant new costs on U.S. banks, not the least of which is reducing the efficient allocation of financial resources and the mobility of capital. It also makes the resolution of failing institutions more difficult. We believe that the FDIC recognizes this, in that, through recognizing a dual payability option, it was trying to assist the industry in addressing the concerns of the UK FSA while not affecting the viability of the branch structure. Yet, ironically, the Proposal has increased the risk that (or at least the uncertainty as to whether) subsidiarization may ultimately have to be used as a solution to foreign deposit subordination.

This risk is not minor. Notwithstanding the fact that the Proposal forces dual pay as the only viable solution to the depositor preference issue, it is unfortunately not yet clear that dual payability will be acceptable as a solution to foreign regulators. While this option was mentioned by the UK FSA in the FSA Consultation Paper and, therefore, may meet the UK FSA's technical expectations, it is not clear that it will be acceptable in all jurisdictions to avoid subsidiarization. Even in relation to the FSA Consultation Paper, discussions by our members, our counsel and our members' counsel with the UK FSA and the Bank of England have surfaced a preference by the U.K. regulators to have this international issue resolved once and for all with a direct, clear, blanket solution, and the U.K. regulators realize that the FDIC's Proposal may yield a suboptimal variety of approaches by different banks, for different customers, or across different jurisdictions.

Furthermore, as dual pay structures are implemented, further hurdles may appear. For example, the numerous contractual issues that must be addressed to implement dual payability

⁴⁰ Banks will have to maintain additional liquidity in both locations, as we understand the FDIC's position to be that depositors should always have access to their assets, including in times of turmoil, and banks cannot be certain in times of turmoil which offices will face increased customer demands.

⁴¹ Of course we are aware that banks have been holding, and will be required to hold under pending or future regulations, appropriate amounts of liquidity and liquidity buffers. We are merely pointing out that a dual pay regime would require additional liquidity, and in more than one currency.

present opportunities for *customers* to reject dual payability as an option.⁴² If some customers reject dual payability and only the portion of a branch's customers that have accepted dual pay are benefiting from depositor preference, it remains an open question whether the UK FSA (or other regulators) will require yet other alternatives to prevent subordination of *all* foreign depositors, such as through subsidiarization.

Thus, the FDIC's belief that the Proposal will, albeit indirectly, resolve the issues raised by the UK FSA and potentially other regulators, could be revealed to be incorrect as implementation progresses. During or after implementation, however, it will be too late to create another solution. The viable possibility of such a major setback should require reconsideration of the Proposal, and the FDIC should seize the opportunity to adopt the recommended combined approach.

Third, the differential implementation across different banks and different national jurisdictions, as noted above, and the significant potential for a myriad of implementation mechanics and local legal requirements imposed on the dual pay solution, present real costs to the banking industry and our customers.

B. By Requiring Restructuring of Client Relationships, the Proposal Imposes on the Industry Multiple Tangible and Intangible Costs

Dually payable deposits are complex and costly for banks to institute. These increased costs and risks also highlight how the FDIC's concerns about a unilateral move by the banks to dual payability are overstated. Therefore, it is not clear to us why banks are being forced into this solution, particularly when there is a better, clearer alternative available for both the FDIC and the industry. A solution based on an interpretation of "deposit liabilities" in FDIA § 11(d)(11) as including foreign deposits would incur none of these costs.

There are a number of tangible and intangible costs to implementing a dually payable deposit structure. First, banks must incur the costs of revising contracts, providing explanations and disclosures, training personnel, and addressing potential customer opt-outs. There are numerous additional potential costs embedded in these contractual modifications. For example, there will be inefficiencies and costs created by having to manage a multitude of different dual pay mechanics and solutions across different jurisdictions or with different customers.

Second, there are likely to be enormous record-keeping and other operational costs. Depending upon whether a contract can limit certain of these operational complexities (see further discussion below), banks may have to establish separate operations in the U.S. to handle potential withdrawal requests in the U.S.; may need to develop systems and liquidity sources for the payment on demand of foreign currencies out of U.S. offices (contrary to most U.S.

⁴² Such customer behavior is both possible and understandable. Customers of U.K. branches have not displayed a desire for dual payability. On the contrary, the increased costs of dual payability for our member institutions are likely to be passed on to customers, and we have seen no evidence that customers would prefer to pay more for the elimination of foreign depositor subordination. There are many additional reasons that customers are expected to object to dual payability, such as potential international tax implications, subjecting transactions in the account to the jurisdiction of the U.S. government, and general confusion related to the change.

branches' current capabilities, even at the largest, most sophisticated banks); will need to monitor diligently to avoid double payments to customers; and will need to establish systems to categorize foreign deposits into demand and time deposits to comply with Regulation D (when such categorization was heretofore unnecessary). Operational complexity will not only affect the conduct of business at the branches today, but would undoubtedly create significant difficulty and unnecessary complexity for the operations of an institution going forward as technology, payments systems, internationalization of business, and customer preferences change. The full extent of these operational issues for the industry and the FDIC has not been fully explored, but there is little doubt that the Proposal will increase costs to regulators, industry, and customers.

Third, there will be a significant loss of competitiveness. Banks competing with U.S. banks will not have to incur the customer confusion and the passing on of costs of dual payability to customers. There is no question that such costs can cause customers to terminate relationships with a U.S. bank. We understand that there are some that would argue that, from the perspective of the banks, being able to pass on these costs in the form of lower interest rates or additional fees would result in cheaper funding through "low cost" deposits. This argument, however, is not relevant. The argument assumes significant inelasticity of demand by depositors. However, that is not the case – depositors have many other choices of international and domestic host country banks, including those that will not have the overhead costs of a dual pay structure. Therefore, there will be a real loss to competitiveness through the adoption of dually payable deposits.

Fourth, the Proposal will increase costs to banks with dually payable deposits by requiring banks to hold greater reserves against demand deposits under the Federal Reserve's Regulation D. Although the Federal Reserve pays interest on reserves, banks incur the opportunity cost of losing potentially greater returns on these idle funds – greater returns that could come through the offer of other products during this historically low-interest environment. As mentioned, to comply with reserve requirements, banks will also have to update operational mechanics to distinguish between demand and time deposits in their records and reports. We also mentioned above the potential opportunity costs of maintaining liquidity in multiple locations for the possibility of withdrawal.

Fifth, significant regulatory reporting modifications will need to be made. Prior to even incurring the costs and tracking for such modifications, however, several reporting requirements will need to be clarified by the FDIC and other U.S. bank regulators. We identify many of these reporting questions in [Appendix C](#).

Sixth, the full extent of tax issues (either to the bank or to the foreign depositors) is not currently estimable and is dependent upon numerous factors that are not conducive to tax certainty in the abstract. At this point, we can only say that dually payable deposits raise tax ambiguities, and therefore potential tax costs, that could be avoided by not requiring deposits to be dually payable. These tax issues have not been adequately considered in the public comment process and regulatory deliberations.

C. The Proposal Raises Several Issues that Require Further Clarification or Regulatory Guidance for the Industry to Implement Dual Pay in a Safe, Sound, and Effective Manner

The Proposal raises a significant number of questions that require clear and direct answers. Although we strongly desire a different outcome, the issues we describe below would arise were the Proposal to be adopted largely unamended. In that case, banks would be required to adopt dual payability for foreign deposits in order to resolve the depositor preference issue.

First and foremost, as a technical matter, the Proposal does not address the UK FSA's concerns about foreign depositor subordination. Regardless of what the preamble to the Proposal may imply, the language of the proposed modification to the FDIC's Part 330 answers only the question of whether dually payable deposits are covered by the U.S. deposit insurance scheme. The banking industry is left to resolve the depositor subordination problem as best it can.

A clearer determination of the depositor preference issue is needed. The regulatory change to the FDIC's Part 330 does not provide us with the solution that we need to bring to the UK FSA and other regulators. Indeed, the FSA Consultation Paper, if eventually enacted as proposed, would conclude that banks "will be required to explain to their FSA supervisors how the chosen measure would operate under the national depositor preference legislation in their home country. Firms will also have to provide legal opinion [sic] on how the measure they are proposing would eliminate the subordination of UK branch depositors."⁴³

Although the banking industry would prefer not to have to employ dual pay, if there is no other choice after finalization of the Proposal, ABA and ABASA believe that the FDIC must provide a legal opinion to the industry, upon which banks, depositors, courts, and foreign governments and regulators can rely, on the efficacy of dually payable deposits in removing the subordination for such foreign deposits under FDIA § 11(d)(11).⁴⁴

Second, the Proposal undermines federal protection of banks from sovereign risk and creates significant uncertainty that must be resolved before the Proposal is finalized. Pursuant to Section 25C of the Federal Reserve Act,⁴⁵ banks are not "required to repay any deposit made at a foreign branch of the bank if the branch cannot repay the deposit due to (1) an act of war, insurrection, or civil strife; or (2) an action by a foreign government or instrumentality (whether de jure or de facto) in the country in which the branch is located; unless the member bank has expressly agreed in writing to repay the deposit under those circumstances." However, the FDIC does not fully address the impact of the Proposal on this provision. The FDIC merely states that "[n]othing in the [Proposal] is intended to preclude a United States bank from protecting itself against sovereign risk by excluding from its deposit agreements with foreign branch depositors

⁴³ FSA Consultation Paper at § 3.12.

⁴⁴ A supporting reason for this request lies in the fact that the Proposal's change to Part 330 is a deviation from the implicit conclusion of the 1994 Advisory Opinion that dually payable deposits are, in fact, "deposits" for purposes of the FDIA. Given this change to the conclusion of the 1994 Advisory Opinion, clarity in the form of a formal opinion is needed as to whether dually payable deposits are also "deposit liabilities" for purposes of Section 11(d)(11) of the FDIA, as implied also by the 1994 Advisory Opinion.

⁴⁵ 12 U.S.C. § 633.

liability for sovereign risk.”⁴⁶ Yet, because the Proposal does not address the depositor preference statute, but only the insurance status of dually payable deposits, there is still ambiguity as to whether a bank’s actions in compliance with Section 25C would have some effect on the ability of the bank to cure the subordination of foreign depositors.

We are extremely concerned that the Proposal’s push toward dually payable deposits as a solution to depositor preference issues actually increases sovereign risk from foreign deposits, including potentially from emerging market branches, and increases the potential for litigation under Section 25C from foreign depositors. Sovereign risk was the major motivation for banks refraining from providing dual payability in the past, even in countries as stable as the U.K. This motivation has not changed.

Therefore, we request two clarifications from the FDIC. First, we request that the FDIC provide an opinion, upon which banks, depositors, courts, and foreign governments and regulators can rely, on whether a deposit that, although otherwise dually payable, excludes payability at a U.S. office during the events described in Section 25C will still be deemed a deposit payable at an office “located in any State” *and* therefore will still be deemed to be a “deposit liability” that retains the benefit of depositor preference under FDIA § 11(d)(11). Second, we request that the FDIC join the industry in seeking an opinion from the Federal Reserve, upon which banks, depositors, and courts can rely, that sets out language which, once inserted into the deposit contract to exclude payability at a U.S. office during the events described in Section 25C, will be sufficient for banks to preserve the protections of Section 25C.

Third, although all of our members are concerned with the Proposal’s impact on the industry’s protection from sovereign risk, there is also a likelihood that various members, for operational and risk management reasons, may impose additional restrictions on a foreign depositor’s ability to withdraw deposits from a U.S. office. For example, in addition to contractually excluding payability during one of the events described in Section 25C, banks may also add one or more of the following restrictions to contracts for foreign branch deposits: (1) deposits will be payable at a U.S. office only if demand has first been made on the foreign office and the foreign office has not paid (except the U.S. office will not pay if the foreign office has not paid because of events described in Section 25C); (2) deposits payable at a U.S. office will only be payable in U.S. dollars at the spot FX rate at the time a request for withdrawal is made; and (3) deposits will be payable only if there is no other impediment placed on payment of the deposit by law or regulation in the host country (such as a security interest, attachment, garnishment, freezing of account, etc.). Because these deposits, therefore, will not be payable in a U.S. office in all circumstances, it is imperative that banks understand whether such deposits will continue to benefit from depositor preference and whether such deposits will satisfy the requirements of the UK FSA and other regulators demanding a solution to the subordination of foreign deposits. We request that the FDIC provide a legal opinion to the industry, upon which banks, depositors, courts, and foreign governments and regulators can rely, on whether deposits with such withdrawal restrictions will still be effective in removing the subordination for such foreign deposits under FDIA § 11(d)(11).

⁴⁶ 78 Fed. Reg. at 11,605.

D. The Lack of a Complete Solution to the Depositor Preference Issue Multiplies the Costs Described Above

The challenges and costs referenced above must be viewed in a broader international context. If the Proposal were to be adopted in its current form, dual pay will become *the only acceptable solution* adoptable by the banks themselves should jurisdictions other than the U.K. require addressing local depositor subordination. Furthermore, we believe that other jurisdictions will evaluate the impact of the FSA Consultation Paper and may enact different proposals as they learn from the U.K. experience (albeit similarly focused on local depositor subordination). Thus, the risks and costs identified in this letter must be *multiplied* by the potential for banks to face this issue across multiple jurisdictions and by the added potential for multiple variations of approach by either (or both) the host jurisdiction or the bank. Further, if a particular jurisdiction does not recognize dual pay as a sufficient solution, then by not creating a regulatory solution directly for the instant problem of depositor preference, banks will be forced to consider subsidiarization in such jurisdictions. This will further create inconsistent approaches and likely regulator and depositor confusion, and will not achieve the mutual goals of the FDIC and financial institutions.

E. These Costs and Inefficiencies Affect Small and Large Banks Alike and Create Barriers to Establishment of New Branches Overseas

The challenges and costs created by the Proposal also will restrict the ability of U.S. banks, of all sizes and charter types, to serve their customers, particularly the growing number of small businesses of all sizes that require a bank to be fluent in international financial transactions. ABA members include community and mid-size banks with overseas branches and transnational operations. While most community and midsized banks with foreign branches did not necessarily feel compelled to respond to the FSA Consultation Paper given other priority issues, they are nevertheless concerned about the UK FSA's action and the reaction of other non-U.K. jurisdictions to the depositor subordination issues. They are also acutely concerned about fixing such issues in a clear and efficient manner and about avoiding regulatory uncertainty. Those banks with branches in the U.K. were directly affected by the FSA Consultation Paper and will need to address, on a more practical level, the uncertainty imposed by the Proposal, and the attendant costs and operational inefficiencies to their U.K. operations, which are likely to be significant, particularly relative to their asset size.

The broader concern is that *any* U.S. bank, large or small, wishing to branch overseas will have to understand new—and potentially conflicting—depositor preference-related standards in each host jurisdiction, and comply with the resulting patchwork of requirements. In other words, adoption of the Proposal would effectively raise the bar for banks that want to develop foreign branch operations. This compliance burden would not be imposed if the recommended combined approach were adopted – *every* branch established overseas would, with certainty of law, extend depositor preference to foreign depositors without the bank having to take additional action or assume additional costs. If the underlying depositor preference issue is not resolved satisfactorily, the resulting complexity and uncertainty will be a barrier to entry for smaller banks and will hinder the expansion of larger banks, to the detriment of small business and global economic activity, generally, and will further inhibit the diversification of the U.S. banking industry.

VI. Conclusion

We believe that there is a better, more direct solution than the Proposal that will eliminate the unintended consequences described in this letter. An interpretation of “deposit liability” in FDIA § 11(d)(11) as including foreign deposits, adopted together with the FDIC Proposal, would be far superior to adopting the Proposal alone. It would offer legal clarity without execution risk and without the unintended consequences caused by requiring adoption of dually payable deposits. The Proposal should be revised and repropose to incorporate this interpretation together with the current proposed rule on insurance of dually payable deposits. This combined approach would resolve the depositor preference issue once, for all foreign jurisdictions, and with the certainty and formality of a fully vetted regulation. We urge the FDIC to adopt this approach.

Not adopting this approach will mean that the final rule has failed to directly address national depositor preference and, therefore, failed to target the root cause of issues like those presented by the FSA Consultation Paper. As described in this letter, such an approach will ironically undercut the evident goals of the Proposal. Risk to the DIF will increase, international cooperation will be impaired, and the main source of contention – U.S. depositor preference – will continue to create international friction. Both the FDIC and the industry will be forced to address repeatedly various questions and implementation issues, because the execution of dually payable deposit structures could vary across banks, across jurisdictions, across customers and over time.

If the Proposal is adopted without inclusion of the proposed interpretation of “deposit liabilities,” we also specifically request that the FDIC (a) provide legal certainty on the various questions on depositor preference and recognition of contractual limitations on dual payability of deposits, as described in Section V.C. above, and (b) continue the dialogue with the industry in order to develop the means to address the variety of risks and costs that will be incurred under the Proposal.

We also draw the attention of the FDIC to the comment letter by The Clearing House, into which many of our members also had input, and which is consistent with the views presented in this letter.

* * *

ABA and ABASA appreciate the opportunity to comment on the Proposal. Should you have any comments or questions, please feel free to contact Wayne Abernathy, at (202) 663-5222, or Cecelia Calaby, at (202) 663-5325.

Very truly yours,



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Federal Deposit Insurance Corporation

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Appendix A

Law Firm Memo

THE STATUS OF FOREIGN BRANCH DEPOSITS
UNDER THE DEPOSITOR PREFERENCE RULE

January 2, 2013

I. Introduction

The status of deposits payable solely in a foreign branch of a U.S. bank (“foreign branch deposits”) has become a central issue in the efforts of the Federal Deposit Insurance Corporation (the “FDIC”) to develop an effective and credible system for resolving a systemically important U.S. bank with significant international operations (“U.S. G-SIB”). This issue has also become a linchpin in achieving international cooperation and coordination in both regulating and resolving global banks.

The three undersigned firms recommend that the FDIC exercise its clear legal authority to issue a formal interpretation or regulation with respect to foreign branch deposits that would effectuate its goals without adverse consequences. Specifically, the FDIC should interpret the term “deposit liability,” as used in Section 11(d)(11) of the Federal Deposit Insurance Act (the “FDIA”),¹ to include all the deposits of a U.S. bank whether made and payable at domestic branches or foreign branches. Under this approach, foreign branch deposits would remain uninsured.²

We have also considered whether the FDIC could adopt an alternative approach of allowing foreign branch deposits to be payable at both a U.S. and foreign branch without becoming insured deposits. For the reasons discussed below, we have concluded that such an

¹ 12 U.S.C. § 1821(d)(11).

² The undersigned law firms believe that this interpretation of “deposit liability” represents the better legal conclusion. It is not necessary, however, to reach such a conclusion in order to determine that the FDIC has the legal authority to define “deposit liability” under Section 11(d)(11)(A)(ii) as inclusive of foreign branch deposits.

approach is less desirable than the one proposed and would involve more complex interpretations by the FDIC and a more difficult legal analysis.

II. Background

In 1993, Congress amended the FDIA to create a Depositor Preference Rule (“DPR”) that provided a national framework for the payment of creditors of a failed insured bank or thrift.³ Before the DPR, all creditors, including the FDIC (as subrogee of insured depositors) and all uninsured depositors, of a failed bank were paid *pari passu*, absent a contrary state depositor preference regime for state banks. Because the DPR statute, however, accords priority to any “deposit liability,” the definition of this term is critical. The plain language of the DPR does not distinguish among depositors, e.g., it is not styled the “Domestic Depositor Preference Rule.” Nonetheless, the FDIA does not provide a definition of “deposit liability” nor does it provide any specific delineation of the distinction between “deposit liability” in Section 11(d)(11) and the defined term “deposit” in Section 3(l) of the FDIA, which excludes foreign branch deposits.⁴

In 1994, then Acting General Counsel Douglas Jones issued an advisory letter opinion (the “1994 Advisory Opinion”) that concluded that the meaning of the term “deposit liability” in Section 11(d)(11) was coterminous with the definition of “deposit” in Section 3(l)(5), at least insofar as excluding foreign branch deposits is concerned.⁵ The effect of the view taken in the 1994 Advisory Opinion is, therefore, to subordinate foreign branch deposits to domestic deposits, making them *pari passu* with general creditor claims. The FDIC, however,

³ Section 11(d)(11) of the FDIA, 12 U.S.C. § 1821(d)(11).

⁴ 12 U.S.C. § 1813(l).

⁵ FDIC Advisory Opinion, “Deposit Liability” for Purposes of National Depositor Preference Includes Only Deposits Payable in U.S., FDIC 94-1 (February 28, 1994) (“‘Deposit liability’ is defined with reference to other provisions of United States law and excludes any obligation payable only outside of the United States and its territories. 12 U.S.C. § 1813(l). Therefore, ‘deposit liability’ under the National Depositor Preference statute does not include obligations payable *solely* at a foreign branch or branches of a United States chartered bank.”) (emphasis in original).

has never issued a binding interpretation of the term “deposit liability,” as used in the DPR statute, through a fully-considered Board of Directors-approved action.

Recent international regulatory developments and policy considerations have made it essential to consider a definitive and reasoned analysis of the status of foreign branch deposits under the DPR. As described below, a determination that “deposit liability” under the DPR statute includes foreign branch deposits would be consistent with the FDIC’s policy goals, would faithfully adhere to the statutory language and legislative history of the DPR statute and would avoid adding further strain on the Deposit Insurance Fund (the “DIF”).

III. Policy Considerations Relating to Foreign Depositor Subordination

In light of the events of the 2008-2009 financial crisis, there has been a growing international consensus recognizing the increasing interconnectedness of global markets and the need for strengthened cross-border regulatory cooperation and consistency, particularly with respect to crisis management and resolution of large, multinational financial institutions. The FDIC itself has been in the forefront of publicly supporting this consensus and has enunciated a policy of increased and improved international cooperation,⁶ and Chairman Gruenberg has been an eloquent spokesman on the necessity for improved cross-border cooperation.⁷

The FDIC’s objective is, however, being undermined by the subordinated treatment of foreign branch depositors under the DPR statute, as interpreted by the 1994

⁶ See, e.g., FDIC and Bank of England, Resolving Globally Active, Systemically Important, Financial Institutions, December 10, 2012 (the “FDIC-BoE Paper”) (“Given the cross-border nature of G-SIFIs, the resolution strategy should ensure financial stability concerns are addressed across all jurisdictions in which the firm operates. To be successful, such an approach will require close cooperation between home and foreign authorities.”).

⁷ See, e.g., Remarks by Martin J. Gruenberg, Acting Chairman, FDIC at the Federal Reserve Bank of Chicago Bank Structure Conference (May 10, 2012) (“Our goal [in reaching out to foreign supervisors and resolution authorities] is to forge a more collaborative process and lay the foundation for more reliable cooperation based on mutual interests in national and global financial stability. The focus of our bilateral discussions has been to identify and mitigate impediments to orderly resolution that are unique to specific jurisdictions and to examine possible resolution strategies and practical issues related to their implementation.”).

Advisory Opinion. For example, the consultation paper (the “FSA Consultation Paper”)⁸ recently issued by the U.K.’s Financial Services Authority (the “FSA”) recognized that “[w]hen host country depositors are treated less favourably, co-operation between host and home country authorities in a resolution could be more challenging.” If, as Chairman Gruenberg has stated, a key element of improving cooperation is elimination of impediments to orderly resolution, then a binding interpretation that eliminates the subordination of foreign branch depositors is needed.

The subordination of foreign branch deposits is also inconsistent with the Financial Stability Board’s “Key Attributes of Effective Resolution Regimes for Financial Institutions” (the “FSB Key Attributes”),⁹ which provide an international standard for the resolution of systemically important financial institutions and which have been endorsed by the G-20 heads of government, including the United States. The principle of non-discrimination for depositors of a bank is stated directly in FSB Key Attribute 7.4:

National laws and regulations should not discriminate against creditors on the basis of their nationality, the location of their claim or the jurisdiction where it is payable. . . . Recognition or support of foreign measures should be provisional on the equitable treatment of creditors in the foreign resolution proceeding.¹⁰

Even more significantly, these multinational governmental initiatives demonstrate that an interpretation of “deposit liability” that excludes foreign branch deposits is an obstacle to the FDIC’s ability to achieve its goal of resolving a U.S. G-SIB on a “single entity” basis—that is, without foreign ring-fencing of foreign branch deposits and assets.¹¹ If the DPR statute is interpreted to continue to discriminate against foreign branch deposits, foreign regulators will

⁸ See U.K. FSA Consultation Paper, Addressing the implications of non-EEA national depositor preference regimes (September 2012) available at <http://www.fsa.gov.uk/static/pubs/cp/cp12-23.pdf>.

⁹ Financial Stability Board, “Key Attributes of Effective Resolution Regimes for Financial Institutions,” (Oct. 2011) (“Recognition or support of foreign measures should be provisional on the equitable treatment of creditors in the foreign resolution proceeding.”).

¹⁰ The divergence between the treatment of foreign branch depositors under the DPR statute, as interpreted by the 1994 Advisory Opinion, and the FSB Key Attributes is particularly problematic because the FDIC has been leading a peer review of progress in implementing the FSB Key Attributes.

¹¹ See FDIC-BoE Paper.

have a powerful incentive to protect “their” depositors from subordination by ring-fencing foreign branch deposits and assets, by resolving foreign branches on a “separate entity” basis and by otherwise interfering with, rather than cooperating with and facilitating, the FDIC’s resolution of a U.S. G-SIB on a “single entity” basis. Although these concerns were relevant when the 1994 Advisory Opinion was issued, the importance of this matter has been sharply magnified in the intervening years, and, indeed, this current situation contrasts with a basic premise of the 1994 Advisory Opinion that subordination supported a single entity approach.¹²

Although the interpretation of the DPR in the 1994 Advisory Opinion has long been raised as a potential impediment to improved cooperation, the issuance of the FSA Consultation Paper now has brought this issue to a head. The FSA Consultation Paper would prohibit the acceptance of deposits at U.K. branches of U.S. banks, unless the disparate treatment of non-U.S. branch depositors is addressed. There are two principal ways for U.S. banks to do this: by restructuring the corporate entity (i.e., through “subsidiarization” of the branch) or by restructuring the client relationship (i.e., by making deposits at those branches payable in the United States). Both methods create negative consequences. The preferable solution is to address the underlying cause—the subordination of foreign deposits—through a formal FDIC interpretation of the DPR statute that makes all uninsured deposits *pari passu*.

Subsidiarization would be detrimental to both the U.S. banking industry and the economy and is an undesirable course from a number of perspectives. Not only will such restructuring impede the flow of capital and liquidity worldwide, but it will significantly reduce U.S. banks’ ability to compete in key markets and retain customers abroad. A foreign branch is backed by the capital, liquidity and operational resources of the overall global bank. This makes

¹² See 1994 Advisory Opinion *supra* note 5 (“United States law applies a ‘single entity’ approach to receiverships of multinational banks chartered within the United States. . . . The adoption of a national depositor preference scheme for the distribution of the assets of a failed insured depository institution does not necessitate a change in the use of the single entity approach in a multinational liquidation.”)

a branch better able to serve the diverse and large credit, payments processing, and other financial services needs of its U.S. and non-U.S. customers than would a separate subsidiary. Subsidiaries simply cannot have the same resources and product suites to support their customers' business needs as the larger global bank, and, if subsidiarization were implemented, customers would be forced to look elsewhere to fulfill these needs.¹³ Subsidiarization also weakens banks that employ such a structure, as individual capital and liquidity becomes trapped in the subsidiary and is often not available to the bank as a whole. Moreover, the creation of a separate deposit-taking subsidiary could involve a lengthy timeline for foreign regulatory approval (if achievable at all) and will subject the bank to separate capital, separate supervision and other regulatory requirements to which a foreign branch of a U.S. bank would not be subject.

If the FDIC does not take action to end foreign branch deposit subordination, increasing regulatory pressure on U.S. G-SIBs to eliminate this discriminatory situation will require U.S. G-SIBs to select the only practical option and make foreign branch deposits dually payable, both at the foreign branch and at an office of the bank in the United States. In doing so, the banks would not merely make foreign branch deposits *pari passu* with domestic deposits, but would cause such dually payable deposits to satisfy the definition of "deposit" under Section 3(l) and also the definition of "insured deposit" under Section 3(m) of the FDIA (subject to the statutory insurance limits).¹⁴ Although this approach eliminates foreign branch deposit subordination, at least as interpreted in the 1994 Advisory Opinion, it would directly expand the FDIC's deposit insurance liability and thus increase the demands on the DIF. Absent a change in statute, regulation or interpretation (all of which are beyond banks' ability to effect unilaterally),

¹³ These consequences are especially significant in light of the FSA Consultation Paper because of the central importance of London as a financial center for the foreign operations of major U.S. banks. Consequently, the U.K. is both the principal focus of FDIC bilateral efforts to enhance coordination and the most significant jurisdiction confronting the issues presented by the DPR statute.

¹⁴ See 12 U.S.C. § 1813(l)(5)(A) and 12 U.S.C. § 1813(m).

the only logical way for a U.S. bank (which seeks to maintain a foreign branch system) to address the significant pressure to correct this situation is through employing dual payability. Yet, there is also no way for a U.S. bank to terminate the subordination of foreign branch deposits without also making those deposits insured, if the FDIC follows the 1994 Advisory Opinion.

During the financial crisis, the FDIC's role in stabilizing the financial industry and resolving hundreds of banks and its emergence as a thought leader for regulatory reform have increased the FDIC's visibility internationally. The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank")¹⁵ enhances the stature and responsibilities of the FDIC in resolving the largest U.S. financial companies under the Orderly Liquidation Authority and instructs the FDIC to coordinate "to the maximum extent possible" with foreign financial authorities as part of its expanded role.¹⁶ It is difficult to imagine a more direct statutory statement of the importance of cross-border cooperation in support of appropriate efforts by the FDIC to remove impediments to the cooperative resolution of covered financial companies.

Thus, the time is appropriate for the FDIC to continue this leadership position by responding in a targeted manner to the concerns of the FSB and the FSA (and, undoubtedly, other jurisdictions). The simple and direct response to these concerns with the DPR would be the adoption, by formal interpretation or rulemaking, of the interpretation proposed in this Memorandum that would end the potential subordination of foreign branch depositors.

IV. Proposed Interpretation of "Deposit Liability"

We submit that it is now essential for the FDIC to issue, as promptly as practical and for the first time, a formal interpretation or regulation defining the term "deposit liability" in Section 11(d)(11) as including foreign branch deposits.

¹⁵ Pub. Law 111-203 (2010).

¹⁶ 12 U.S.C. § 5390(a)(1)(N).

As discussed below, a textual analysis of Section 11(d)(11), as well as basic statutory interpretation guidelines and the legislative history of the DPR statute, indicates that the most legally sustainable interpretation of “deposit liability” includes all deposits of a bank, both domestic and foreign branch deposits. This analysis also demonstrates that the interpretation from the 1994 Advisory Opinion that the terms “deposit liability” and “deposit” are coterminous is not compelled by the FDIA.

Moreover, the 1994 Advisory Opinion does not preclude the FDIC from adopting, for the first time, a binding determination or interpretation that the term “deposit liability” includes foreign branch deposits under the DPR statute. Indeed, as discussed below, the absence of consideration of alternative approaches and limited discussion of the relevant statutory provisions in the 1994 Advisory Opinion raise a question as to whether it would be accorded judicial deference if challenged. Furthermore, because the 1994 Advisory Opinion was not a formal, numbered General Counsel opinion and it is our understanding that it was never approved by the FDIC Board, there has never been a binding interpretation by the FDIC of the meaning of “deposit liability” in the DPR.

The contrary positions taken by other regulators at the time of the 1994 Advisory Opinion regarding the definition of “deposit liability” and the analysis below demonstrate that this term is, at a minimum, ambiguous. The FDIC has ample authority to resolve this ambiguity by adopting the better, and in any case, entirely reasonable, interpretation that foreign branch deposits constitute a “deposit liability” under the DPR statute. This interpretation is fully consistent with the statutory provisions and will advance the key FDIC policy objectives discussed above (advancing international regulatory cooperation and coordination of cross-border resolutions, avoiding ring-fencing of U.S. bank branches overseas, promoting the FDIC’s preferred resolution approach and avoiding both increased demands on the DIF and potentially

serious negative consequences to U.S. banks that would follow from banks using dual payability to solve foreign branch deposit subordination). A determination made in the context of these supporting considerations would be entitled to judicial deference under clearly established precedent.

V. Legal Analysis

An interpretation of “deposit liability” that includes all deposits of a bank, both domestic deposits and foreign branch deposits, is consistent with the plain meaning of “deposit liability,” the usage of this term elsewhere in the FDIA, the legislative history of the DPR statute and the FDIC’s subsequent use of the term “deposit liability” in its regulations.¹⁷ This interpretation advances the FDIC’s policy objectives discussed above while avoiding negative consequences to the FDIC and to U.S. banks.

A. Plain Meaning

Because the term “deposit liability” is not defined in the FDIA, it is appropriate to look first to its plain meaning. This term has no inherent geographic limitation and therefore should be interpreted to include a deposit liability booked in a foreign branch of a U.S. bank absent compelling evidence to the contrary.

The term “deposit liability” should not be bound by the limitation elsewhere in the FDIA on the scope of the different term “deposit.” It is a fundamental tenet of statutory interpretation that different terms used in the same statute should have different meanings.¹⁸ Further, if “deposit liability” were interpreted to mean “deposit,” the word “liability” in “deposit liability” would be mere surplusage. As the Supreme Court has stated: “It is a cardinal principle

¹⁷ 12 C.F.R. § 360.9(b)(2).

¹⁸ The Supreme Court has affirmed “the usual rule that ‘when the legislature uses certain language in one part of the statute and different language in another, the court assumes different meanings were intended.’” Sosa v. Alvarez-Machain, 542 U.S. 692, 711 n. 9 (2004) (citing 2A N. Singer, Statutes and Statutory Construction § 46:06, p. 194 (6th rev. ed. 2000)). See also Mohamad v. Palestinian Authority, 132 S. Ct. 1702, 1708 (2012) (“We generally seek to respect Congress’ decision to use different terms to describe different categories of people or things.”) (citing Sosa at 711 n. 9 (2004)).

of statutory construction that a statute ought, upon the whole, to be so construed that, if it can be prevented, no clause, sentence, or word shall be superfluous, void, or insignificant.”¹⁹

When adopting the DPR statute, Congress knew the term “deposit” existed in the FDIA and could have used that term, but it instead chose “deposit liability.” The fact that Congress chose to use “deposit liability” strongly suggests that Congress did not intend “deposit liability” to be coterminous with “deposit.” The definition of “deposit” pre-dated the DPR and was clearly designed to address the other specific uses of the term “deposit” inherent within the FDIA, such as deposit insurance coverage.

Section 3(1)(5) itself also uses the term “deposit liabilities” but it certainly does not suggest that the two terms (“deposit” and “deposit liability”) are to be defined identically. If the two terms had the same meaning, there would have been no need to use both. Rather, the use of the term “deposit liability” implicitly recognizes that the term “deposit liability” naturally would encompass foreign branch deposits while the term “deposit” does not.

At the very least, however, the use of a different term creates ambiguity, and the FDIC has clear regulatory authority to define the two terms differently.

B. Use of “deposit liability” in the FDIA

Another tenet of statutory construction is that a word used in one place in a statute should be construed consistently with its use in other places in the statute, unless there is a clear indication that Congress intended otherwise.²⁰ “Deposit liability” or “deposit liabilities” (or the term “liability” in the context of deposit liabilities) is used in multiple sections of the FDIA. In

¹⁹ TRW Inc. v. Andrews, 534 U.S. 19, 31 (2001) (internal quotation marks omitted) (quoting Duncan v. Walker, 533 U.S. 167, 174 (2001)). See also U.S. v. Menasche, 348 U.S. 528, 538–539 (1955) (“It is our duty ‘to give effect, if possible, to every clause and word of a statute.’” (quoting Montclair v. Ramsdell, 107 U.S. 147 (1883))); U.S. v. Nordic Village Inc., 503 U.S. 30, 36, (1992) (describing the “settled rule that a statute must, if possible, be construed in such fashion that every word has some operative effect.”) (citing Hoffman v. Connecticut Dept. of Income Maintenance, 492 U.S. 96 (1989)).

²⁰ “[T]here is a natural presumption that identical words used in different parts of the same act are intended to have the same meaning.” Atlantic Cleaners & Dyers v. U.S., 286 U.S. 427, 433 (1932).

none of those instances is it apparent, nor are we aware of any interpretation suggesting, that foreign branch deposits are, were intended to be or should be excluded from the term “deposit liability” as used in these sections. Rather, in some cases, the exclusion of foreign branch deposits would be illogical and contrary to long-established practice. In all cases, the usage of the term “liability” suggests a plain-meaning definition more expansive than a definition of “deposit” from which foreign branch deposits are excluded. For example:

1. 12 U.S.C. §§ 1817(a)(1) & 1817(a)(2)(A): This section authorizes the FDIC to obtain call reports from banks and provides that the reports of condition must include “deposit liabilities.” The FDIC and other federal banking agencies have long interpreted this reference to “deposit liabilities” as including foreign branch deposits. For example, the general instructions for Schedule RC-E to the call report relating to deposit liabilities refer to both domestic deposits and foreign branch deposits as “deposit liabilities.”²¹ Moreover, it would be nonsensical to exclude foreign branch deposits.

2. 12 U.S.C. §§ 1828(a)(4)(A) & (B): This section prohibits false advertising regarding FDIC insurance and misrepresentation of insured status with respect to any “deposit liability.” It is improbable that the FDIC would take the position that this prohibition does not apply to deposits at foreign branches. Rather, these provisions would be most applicable in the case of uninsured deposits, including foreign branch deposits.

3. 12 U.S.C. § 1823(c)(4)(E)(iii): This section clarifies that, notwithstanding other provisions in the FDIA, purchase and assumption transactions (“P&A Transactions”) involving banks for which the FDIC is appointed receiver may include “uninsured deposit liabilities” of the institution as long as the FDIC does not incur a loss with respect to “such

²¹ “Part I [of the instructions] covers the deposit liabilities of the domestic offices of the consolidated bank. Part II covers the deposit liabilities of the foreign offices . . . of the consolidated bank.” FFIEC: Reports of Condition and Income Instructions, Schedule RC-E, Deposit Liabilities (last updated September 2012).

deposit liabilities.” This provision appears designed to avoid any implication that the prohibition on increasing losses to the DIF through covering uninsured depositors or other creditors (12 U.S.C. § 1823(c)(4)(E)(i)) would impair the FDIC’s flexibility in arranging P&A Transactions. Given the relationship between these provisions, it is virtually inconceivable that Congress intended to restrict the FDIC from including foreign branch deposits in P&A Transactions if such inclusion would benefit the DIF.

4. 12 U.S.C. § 1828(c)(1)(B): In the Bank Merger Act provisions of the FDIA, Congress provides that one type of transaction requiring prior regulatory approval is a transaction in which a bank “assume[s] liability to pay any deposits (including liabilities which would be ‘deposits’ except for the proviso in section 1813(l)(5) of [title 12 of the U.S. Code]) made in, or similar liabilities of, any noninsured bank or institution.”²² In this context it is clear that the term “liability” or “liabilities” refers to a broader range of deposit types than merely the term “deposits” as more narrowly defined in Section 3(l) of the FDIA. Indeed, in this provision, Congress has made clear that when it used the term “liability to pay deposits” it meant to include foreign branch deposits.

C. Legislative History

1. The Decade Lead-Up to the DPR Statute

In the early 1980s there was considerable discussion regarding the need to increase market discipline to help reduce the potential losses to the FDIC as a result of bank failures.²³ To this end, there was significant consideration of providing a depositor preference in liquidation over general creditors, both at the federal and state level. The reasons for depositor preference were many and varied, yet none of the discussions focused on a depositor preference

²² 12 U.S.C. § 1828(c)(1)(B).

²³ See James A. Marino and Rosalind L. Bennett, The Consequences of National Depositor Preference, FDIC Banking Review 12, no. 2, at 22. (Oct. 1999) available at http://www.fdic.gov/bank/analytical/banking/1999oct/2_v12n2.pdf.

distinction between foreign branch deposits and domestic branch deposits, other than to describe, in one case, the uninsured status of, and lack of assessments against, foreign branch deposits.

In 1983, the FDIC submitted a study to Congress that addressed matters relating to the future of federal deposit insurance.²⁴ In that report the FDIC first presented publicly the case for the adoption of national depositor preference and spoke only of creating a preference for depositors, generally, and in no way indicated that foreign branch depositors should be excluded from the class of deposits that would receive a preference.²⁵ The FDIC argued that depositor preference would (i) increase market discipline by increasing the potential losses to nondeposit creditors²⁶ and (ii) facilitate the use of the payoff/cash-advance option in handling bank failures by creating more certainty with respect to the amount of funds due to uninsured depositors.²⁷ The FDIC had an additional reason for advocating for NDP. The contingent claims facing a failed bank (e.g., standby letters of credit, loan commitments and potential legal claims) were often difficult to calculate and could be considerable. Without depositor preference, the FDIC was required to treat such claims equally with deposits and, thus, ensure they were paid in full in a P&A Transaction, which transactions were favored by the FDIC because they reduced costs to the DIF.

²⁴ A Report to Congress on Deposit Insurance, Deposit Insurance in a Changing Environment, S. Pet. 98-65 (April 15, 1983).

²⁵ Shortly after publication of the FDIC study, FDIC Chairman William Isaac appeared before the Senate Banking Committee to discuss various reforms proposed by the FDIC and reiterated the benefits of the depositor preference proposal in the FDIC's study. He discussed the proposal in terms of a preference for "depositors" generally. Chairman Isaac did state that, should depositor preference be adopted, "it would be necessary to spell out carefully through legislation who would be preferred." Financial Services Industry—Oversight, Part I, 98th Cong. 111–136 (April 27, 1983) (statement of William M. Isaac, Chairman, FDIC, Senate Comm. on Banking, Housing and Urban Affairs).

²⁶ "[T]hose claims which are generally categorized as 'contingent' should be subordinated to depositors. These might arise, for instance, in connection with standby letters of credit and nonperformance by the failing bank with respect to commitments or loan participations....If depositors were preferred to these claimants, the latter would have to be more concerned about whom it does business with, provides guarantees, etc. The FDIC believes that such increased concern would be appropriate and would act as a check on bank risk in some areas." Id. at 81–82.

²⁷ Id. at 82.

In 1986, during Senate hearings discussing possible financial services reforms, FDIC Chairman L. William Seidman appeared before the Senate Banking Committee to discuss deposit insurance reform.²⁸ After discussing the depositor preference regime that the FDIC had proposed in 1983 in general and broad terms (“depositors” v. “nondeposit claimants”), Chairman Seidman discussed foreign branch deposits in the context of depositor preference directly (this is the only instance in the legislative history of the DPR statute that we are aware of in which foreign branch deposits were mentioned). Chairman Seidman stated:

If we prefer foreign deposits to other bank creditors like domestic deposits, they should be subject to insurance assessments. An alternative would be to prefer domestic deposits and not subject deposits in foreign branches to assessment. (emphasis in original).²⁹

Despite Chairman Seidman’s brief reference to foreign branch deposits, the subsequent questions raised by the Senators on the Banking Committee and Chairman Seidman’s responses did not distinguish between domestic and foreign branch depositors but focused on the distinction between all depositors and contingent/other nondeposit creditors.³⁰ Moreover, Chairman Seidman’s predicate for treating foreign branch and domestic branch deposits alike—equality of assessments—has now been established, in effect, by Section 331(b) of Dodd-Frank.³¹

By 1989, Congress had taken no action to enact a depositor preference regime.

As part of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989

²⁸ Deposit Insurance Reform and Related Supervisory Issues Part II, 99th Cong. 203, 237–291. (March 13, 1986) (statement of L. William Seidman, Chairman, FDIC, Senate Comm. on Banking, Housing and Urban Affairs).

²⁹ Id. at 243.

³⁰ For example, in response to a question from Senator D’Amato, Chairman Seidman stated: “Putting these contingency creditors along with other nondeposit creditors below depositors could significantly lessen FDIC costs and reduce the uncertainty associated with P&A transactions.” Id. at 291; and in response to a question from Senator Proxmire, Chairman Seidman stated “[t]he FDIC continues to favor depositor preference which would place all nondeposit creditors of banks at considerable risk.” Id. at 581.

³¹ As a result of Section 331(b) of Dodd-Frank, FDIC insurance assessments are now based on the average total consolidated assets of a bank (less its average tangible equity), which has the effect of subjecting the foreign branch deposits of U.S. banks to insurance assessments.

(“FIRREA”), Congress did, however, grant the FDIC authority to treat deposit and nondeposit creditors differently, for example, by structuring a P&A Transaction that resulted in making all insured and uninsured deposits whole, as long as nondeposit creditors received at least as much as they would have received in liquidation.³²

2. Enactment of the DPR Statute

On August 10, 1993, as part of the Omnibus Budget Reconciliation Act of 1993 (the “1993 Act”),³³ without public debate and with limited legislative history, Congress amended the FDIA to promulgate the DPR.³⁴ The DPR statute created a uniform federal system for the distribution of assets upon the liquidation of a federal or state bank (thus the often-used term, “national” depositor preference).³⁵ Prior to the DPR statute, the order of priority in the distribution of the assets of a failed bank was determined according to the law of the jurisdiction that chartered the bank.

Contemporaneous observers recognized that Congress’s primary motivation in enacting the DPR statute was budgetary, given the cost savings to the FDIC the Congressional Budget Office had projected. Not surprisingly, therefore, the legislative history of the 1993 Act discusses the DPR in only a few instances. In each of these instances, there is no indication that foreign branch depositors or any other class of depositors was intended to be excluded from the general class of depositors that are entitled to depositor preference.

³² This authority was included in Section 212(a) of FIRREA, which added Section 11(i)(a) to the FDIA. That section provides that the maximum liability of the FDIC to a person having a claim against an insured institution is the amount the claimant would have received had the FDIC liquidated the institution. It effectively allows the FDIC to discriminate among creditors within the same class, subject to a minimum recovery right of liquidation value. The FDIC was previously subject to a pro rata distribution rule that required it to treat similarly situated creditors equally. Tellingly, nothing in Section 11(i)(a) suggests that the FDIC would be entitled to subordinate foreign branch deposits in exercising this authority.

³³ Pub. Law 103-66, 107 Stat. 312 (1993).

³⁴ 12 U.S.C. § 1821(d)(11).

³⁵ Id.

To the contrary, the legislative history strongly supports a broad reading of “deposit liability” that includes foreign branch deposits. For example, the House Budget Committee Report to Congress stated in the section entitled “Explanation of the Legislation” that the DPR statute “amends the [FDIA] to require receivers of failed insured depository institutions to give priority to depositors over general creditors when distributing assets of failed banks and thrifts.”³⁶ The report continued with language that explicitly refers to “all” depositors:

This means that proceeds from the sales of assets in the future would first go to all depositors—the FDIC or RTC (in place or [sic] insured depositors) and uninsured depositors. Only when all depositors have recovered 100 percent of losses would general creditors recover anything. . . . As a result of this depositor preference, creditors who are not depositors are unlikely to recover any of their claims on failed institutions.” (emphasis added).³⁷

The report of the House and Senate Conference Committee used similarly broad and general language to describe the preference for depositors under the DPR statute.³⁸

This provision amends the [FDIA] to give depositors a preference over general and subordinated creditors and shareholders when a receiver distributes assets from failed banks and thrifts.

In seeking to accomplish this objective, Congress intended to follow the practices of 29 states that had adopted depositor preference statutes by 1993. In a statement on the House floor following presentation of the Conference Report to the House, Representative Gonzalez spoke on behalf of the House Banking Committee:

Mr. Speaker, the Committee on Banking, Housing and Urban Affairs met its over \$3 billion in budget savings through a variety of measures. On the banking side, the committee endorsed the practice of 29 States by adopting a Federal deposit preference scheme. (emphasis added).³⁹

³⁶ House Budget Committee Report, HR 103-111, at 85 (May 25, 1993). It is not clear what the Committee meant by the reference to “general creditors” because all depositors are general creditors, but there is no basis for reading this language as departing from the normal meaning of “depositors” and somehow defining foreign branch depositors as general creditors rather than depositors.

³⁷ Id. at 95.

³⁸ See Conference Report, HR 103-213, at 436–7 (August 4, 1993).

³⁹ 103 Cong. Rec. H6150 (August 5, 1993).

An analysis of the state statutes that Congress sought to replicate provides further support for the conclusion that Congress did not intend to distinguish between foreign and domestic branch depositors. Of the 29 states with depositor preference statutes at the time of the 1993 Act, the depositor preference statute of the one state with a number of banks that had foreign branch deposits, California, expressly included foreign branch deposits in the preference for depositors, even though California borrowed part of the Section 3(l) definition of “deposit” in the FDIA.⁴⁰ The depositor preference statutes in 26 of the remaining 28 states gave no indication that foreign branch deposits were intended to be excluded from the benefit of priority. Almost all the depositor preference regimes in these states used broad, general language to describe the class of depositors that would benefit from priority (e.g., deposits, claims of depositors, debts due depositors, deposit obligations) and either did not define the general terms used or the definition itself implied a broad construction (e.g., “Depositor” defined as “any person who deposits money”). Indeed, in one of these states, New Hampshire, the statute was quite clear that the term deposit was not limited to the definition of “deposit” in Section 3(l) of the FDIA.⁴¹ Two of the 29 states, Florida and Rhode Island, gave priority to “deposits” and defined deposits by reference to Section 3(l), without anything further. It is unclear whether these two states intentionally decided to exclude foreign branch deposits of banks or simply chose a readily available definition of a term that is difficult to define.⁴²

⁴⁰ Westlaw Annotated CA Financial Code, Section 3119.5(a)(3) (1993) (“claims for ‘deposits,’ as that term is defined in 12 U.S.C. Section 1813(l), but including obligations of the type described in 12 U.S.C. Section 1813(l)(5)(A) and (B)”).

⁴¹ Westlaw NH Statutes Annotated, Section 395:30(III) (1993) (“deposit accounts including but not limited to ‘deposits’ as defined in 12 U.S.C. section 1813(l), or as it may be later amended from time to time”).

⁴² We have found no legislative history on the deposit preference laws in Florida and Rhode Island that would provide any indication regarding the intent of their respective legislatures.

D. Policy Considerations

1. The Proposed Interpretation Avoids Negative Consequences that Result from Dual Payability

As discussed above, without FDIC action to end foreign depositor subordination under the DPR, the only logical option for U.S. banks to address this issue would be to make foreign branch deposits dually payable in the United States and in the foreign branch, thereby converting the foreign branch deposit into a “deposit” and an “insured deposit” under the FDIA. If most U.S. banks were to choose this option, a number of negative consequences, both for the FDIC and for U.S. banks, would result.

With respect to the FDIC, dual payability could cause a significant increase in claims on the DIF. This is particularly the case in jurisdictions where U.S. banks have a retail banking presence.⁴³ Additionally, increasing the number and amount of insured foreign branch deposits will expose the FDIC to increased costs and administrative difficulties in administering overseas payouts in the event of a payout of insured foreign branch deposits.

If the FSA implements the FSA Consultation Paper, we think it is almost inevitable that other jurisdictions will take similar action. Even if, however, the practice of making foreign branch deposits insured were limited to branches located in the U.K., there is a significant risk that, in a failure, other foreign jurisdictions would implement ring-fencing or other similar methods to carve out assets of branches of U.S. banks and otherwise resolve such foreign branches on a “separate entity” basis. Any such actions would significantly complicate the FDIC’s resolution of the failed bank and interfere with its goal of resolving the bank on a “single entity” basis in order to preserve the bank’s franchise value, minimize losses and

⁴³ As is the case with domestic depositors, foreign depositors will undoubtedly structure their deposits in such a way as to have FDIC insurance for a multiple of the \$250,000 single account maximum.

otherwise promote U.S. and global financial stability, and they are likely to decrease substantially the assets available to the FDIC as part of the resolution.

As a systemic matter, the subordination of foreign branch deposits also increases the liquidity risk for banks, and could even precipitate a bank failure, as subordinated foreign branch depositors have a strong incentive to flee if there are actual or perceived concerns about the bank's viability or even concerns about the banking industry more generally.⁴⁴ This risk is increased to the extent the issue of subordination continues to be highlighted by foreign regulators and the news media. These issues were brought to the fore during the 2008-09 financial crisis amid concerns about the potential for panic-induced responses by foreign depositors. Indeed, for these reasons and the possibility of ring-fencing, the FDIC itself has concluded that the subordination of foreign branch deposits under the DPR statute does not provide any appreciable benefit to the FDIC in terms of loss absorption in the event of a bank failure, in large part because of this flight risk.⁴⁵

From a U.S. bank's perspective, making deposits payable in the United States may eliminate the protections for the bank in Section 25C of the Federal Reserve Act⁴⁶ that limit the ability of foreign branch depositors to demand payment in the United States when actions by

⁴⁴ Marino and Bennett, *supra* note 23, 19–38 (concluding based on empirical analysis, that, even before the DPR statute was enacted, foreign branch depositors generally tended to flee foreign branches as a bank became stressed, to a greater degree than domestic depositors, and suggesting that the greater incentive created by the DPR statute would exacerbate that reaction).

⁴⁵ 76 Fed. Reg. 10672, 10681 (Feb. 25, 2011). In its final rule implementing changes to FDIC insurance assessments required by Section 331(b) Dodd-Frank, the FDIC rejected commenter proposals to factor into the unsecured debt adjustment (an adjustment that would reduce an institution's insurance assessments) the fact that foreign branch deposits are subordinate to the FDIC in liquidation, concluding that such subordination would not provide any appreciable cushion to absorb losses. “[T]he FDIC does not agree that unsecured debt should include foreign office deposits, since there is likely to be a significant reduction in these deposits by the time of failure. In addition, while, under U.S. law, foreign deposits are subordinate to domestic deposits in the event an institution fails, they can be subject to asset ring-fencing that effectively makes them similar to secured liabilities.”

⁴⁶ 12 U.S.C. § 633(a). Section 25C makes clear that a member bank is not required “to repay any deposit made at a foreign branch of the bank if the branch cannot repay the deposit due to— 1. an act of war, insurrection, or civil strife; or 2. an action by a foreign government or instrumentality (whether de jure or de facto) in the country in which the branch is located; unless the member bank has expressly agreed in writing to repay the deposit under those circumstances.”

a foreign government or *force majeure* prevent payment at the foreign branch of the bank. This would undermine the U.S. public policy interest in requiring foreign branch depositors to bear the sovereign risk of the country in which the foreign branches are located, absent express agreement to the contrary. Dual payability will also result in the bank's losing the exemption from the reserve requirements for those deposits under Section 19(b)(6) of the Federal Reserve Act⁴⁷ and Regulation D.⁴⁸ These costs, as well as certain additional implementation costs and burdens, discussed further in Section VIII below, would either have to be absorbed by the affected banks or passed on to customers, in either case, resulting in a potentially adverse impact on competitiveness of U.S. G-SIBs.

Absent adoption of the proposal in this Memorandum, U.S. banks will inevitably be confronted with the need to choose among withdrawing from foreign countries, subsidiarization and dual payability. This selection among undesirable options, and all the above negative effects for U.S. banks and the FDIC, could be avoided by a determination that a foreign branch deposit is a "deposit liability" for purposes of Section 11(d)(11), but continues not to be a "deposit" for purposes of Sections 3(l) and 3(m).

2. The Proposed Interpretation is Consistent with the Principles Expressed in Dodd-Frank

Dodd-Frank altered the assessment base for purposes of calculating FDIC insurance assessments.⁴⁹ Prior to Dodd-Frank, FDIC insurance assessments were based on a bank's total deposits, as "deposit" is defined in Section 3(l), and, therefore, foreign branch deposits were excluded from the calculation of insurance assessments. Section 331(b) of Dodd-Frank required the FDIC to change the assessment base to be the average total consolidated

⁴⁷ 12 U.S.C. § 461(b)(6) ("The [reserve requirements] shall not apply to deposits payable only outside the States of the United States and the District of Columbia....").

⁴⁸ 12 C.F.R. § 204.1(c)(5) ("The provisions of this part do not apply to any deposit that is payable only at an office located outside the United States.").

⁴⁹ Section 331(b) of Dodd-Frank (to be codified at 12 U.S.C. § 1817(nt)).

assets of a bank (less average tangible equity) and, thereby, has the effect of no longer excluding foreign branch deposits from insurance assessments. The proposed interpretation of “deposit liability” under the DPR statute would, therefore, be consistent with the current assessment approach.

E. The Proposal Is Not Precluded by the 1994 Advisory Opinion

The FDIC retains full authority to adopt the initial binding interpretation of the meaning of “deposit liability” under the DPR statute. The ambiguity apparent in the statute, important policy considerations, and an apparently contradictory FDIC regulation provide strong grounds for a definitive declaration by the FDIC. Such an interpretation would be the FDIC’s first formal interpretation of “deposit liability” under the DPR statute. Furthermore, as discussed above, developments internationally since 1994 have significantly altered the international landscape and the policy considerations that the FDIC must address today, including changes in a basic policy premise of the 1994 Advisory Opinion. These factors support a different conclusion than the one reached in the 1994 Advisory Opinion. The Supreme Court has consistently upheld agencies’ authority to change interpretive course in light of changed circumstances or changed views regarding public policy considerations.⁵⁰

As an initial matter, the 1994 Advisory Opinion is not a binding determination or interpretation by the FDIC. The 1994 Advisory Opinion was not a formal, numbered General Counsel opinion, and it is our understanding that the opinion was never approved by the FDIC Board. As a result, a binding determination or interpretation by the FDIC Board would represent the first formal FDIC interpretation of the meaning of “deposit liability.”

Moreover, as discussed above, there are sound legal interpretations of “deposit liability” contrary to the 1994 Advisory Opinion that, we submit, provide a better synthesis of

⁵⁰ See discussion infra Section VI.B.

the relevant statutory provisions. We understand that these contrary interpretations were discussed by the FDIC with other regulators prior to the 1994 Advisory Opinion, but were not addressed in that opinion. Given these alternative opinions, it is not clear that the 1994 Advisory Opinion would be entitled to deference if subjected to judicial challenge because the opinion was issued without any discussion of the alternative interpretations⁵¹ and with limited explanation for its ultimate conclusion. Courts will set aside agency interpretations when an agency has failed to offer a reasoned basis for its conclusion, relied on inaccurate assumptions or failed to consider other possible alternatives to the agency's interpretation.⁵²

The 1994 Advisory Opinion begins with the assertion that “deposit liability” under Section 11(d)(11) “is defined with reference to other provisions of United States law.” It is unclear what was meant by this assertion because neither “deposit liability” nor any other relevant provision of Section 11(d)(11) references “other provisions” of United States law. If it meant that “deposit liability” should be defined consistently with other provisions of the FDIA, the assertion does not support the opinion's conclusion because, as discussed above, “deposit liability/liabilities,” as used elsewhere in the FDIA, has not been interpreted coterminously with “deposit,” a key point that the 1994 Advisory Opinion does not address.

The 1994 Advisory Opinion also assumed that its interpretation would not result in a change in the FDIC's ability to resolve an insured bank with cross-border operations on a “single entity” basis.⁵³ If that assumption were true in 1994, it is demonstrably inaccurate today. As discussed in Section III above, an interpretation of “deposit liability” that excludes foreign

⁵¹ Prior to the issuance of the 1994 Advisory Opinion, we understand that the Federal Reserve Bank of New York and the Bank of England expressed concern over an interpretation of “deposit liability” in the DPR statute that would exclude foreign branch deposits on both textual and policy grounds. The 1994 Advisory Opinion made no attempt to address these concerns.

⁵² See, e.g., *Petroleum Communications, Inc. v. F.C.C.*, 22 F.3d 1164, 1172 (D.C. Cir. 1994) (“Where the agency has failed to provide a reasoned explanation, or where the record belies the agency's conclusion, [the court] must undo its action.”).

⁵³ See *supra* note 12.

branch deposits provides foreign regulators with a powerful incentive to interfere with, rather than cooperate with and facilitate, the FDIC's resolution of a U.S. G-SIB on a "single entity" basis (i.e., through ring-fencing or otherwise).⁵⁴

Further underpinning a need for a formal definition of the term "deposit liability," the FDIC has recognized the breadth of the term in contexts other than the 1994 Advisory Opinion. In a recent rulemaking regarding large bank resolutions, the FDIC defined the term "foreign deposit" in Section 360.9(b)(2) of its regulations by stating that it is a "deposit liability maintained in a foreign branch" of a bank. This definition suggests that foreign branch deposits are one type of the broader term "deposit liability," i.e., those maintained in a foreign branch.⁵⁵ In the related release and in several other instances, however, the FDIC has referred to foreign branch deposits as subordinate to domestic deposits in liquidation, apparently deferring to the 1994 Advisory Opinion, but there has never been any formal articulation of this position or any explanation of the rationale.⁵⁶ Indeed, in these instances, in contrast to the considerations described in this Memorandum, there was likely no compelling reason for the FDIC to revisit the 1994 Advisory Opinion.

The apparent conflict with the use of "deposit liability" in Section 360.9(b)(2) and the 1994 Advisory Opinion, the significantly changed circumstances since the 1994 Advisory Opinion was issued, and the risk that the 1994 Advisory Opinion may not be afforded judicial deference if challenged confirm the need for adoption now of a formal FDIC interpretation of "deposit liability" under the DPR statute.

⁵⁴ We also note that the interpretation proposed in this Memorandum would not change the responses to the questions that were posed to the FDIC and that were addressed in the 1994 Advisory Opinion, i.e., none of the clearing mechanisms used for a deposit, the currency of a deposit or the nationality or residence of the payee would affect the deposit's status under the DPR.

⁵⁵ 12 C.F.R. § 360.9(b)(2).

⁵⁶ See e.g., 73 Fed. Reg. 41180, 41180 (July 17, 2008); 74 Fed. Reg. 5797, 5798 n. 5 (Feb. 2, 2009); 76 Fed. Reg. 10672, 10681 (Feb. 25, 2011); and FDIC Financial Institution Letter, Deposit Insurance Options Paper, FDIC 61-2000 (Sept. 11, 2000).

VI. Deference Due FDIC Interpretation

As discussed above, a textual analysis and the legislative history of the DPR statute indicate that the best interpretation of “deposit liability” in Section 11(d)(11) includes foreign branch deposits. If the FDIC adopts the position that the term “deposit liability” is susceptible to more than one interpretation (*i.e.*, the definition proposed in this Memorandum that includes foreign branch deposits and the definition suggested in the 1994 Advisory Opinion that excludes foreign branch deposits), the term would be ambiguous and the FDIC has ample regulatory authority to select one of the possible interpretations of the term.

It is clear that Congress has granted the FDIC the statutory authority to interpret the FDIA to promote that statute’s objectives and specifically to interpret the DPR statute,⁵⁷ and the Supreme Court has consistently afforded Chevron⁵⁸ deference to agencies, and in particular, the Federal banking agencies, when interpreting ambiguous statutory terms. For a unanimous court, Justice Scalia stated: “It is our practice to defer to the reasonable judgments of agencies with regard to the meaning of ambiguous terms in statutes that they are charged with administering.”⁵⁹

A. Deference under Chevron, Generally

Under Chevron, courts will defer to an agency’s interpretation of a statute if (i) there is an ambiguity and (ii) the agency’s interpretation is a “permissible construction of the statute” (*e.g.*, it is a reasonable policy choice for the agency to make, given more than one possible construction).

⁵⁷ Section 9(a)(Tenth) of the FDIA gives the FDIC the authority to “prescribe by its Board of Directors such rules and regulations as it may deem necessary to carry out the provisions of [the FDIA].” 12 U.S.C. § 1819(a)(Tenth). In addition, Section 11(d)(1) of the FDIA specifically provides the FDIC with the authority to interpret the DPR statute as part of the conduct of receiverships.

⁵⁸ Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984).

⁵⁹ Smiley v. Citibank (South Dakota), N.A., 517 U.S. 735, 739 (1996) (citing Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984)).

As discussed above, there is no clear indication in the statute or in the legislative history that foreign branch deposits should be excluded from the term “deposit liability” in the DPR statute. Congress has not spoken directly on this particular question. If anything, the legislative history and use of “deposit liability” in the FDIA suggest that it would be more appropriate to include foreign branch deposits in the term “deposit liability.” At a minimum, however, the approach proposed in this Memorandum to defining “deposit liability” is a “permissible construction of the statute” because including foreign branch deposits liabilities within the term “deposit liability” in the DPR statute is a possible and legitimate reading of the statute and a reasonable policy choice for the FDIC to make (i.e., this approach advances the positive consequences and avoids the negative consequences noted above).

B. Deference under Chevron for Changes in Interpretation

Although the definition proposed in this Memorandum would be inconsistent with the 1994 Advisory Opinion, the 1994 Advisory Opinion was not a formal, Board-approved action. Under our suggested approach, the FDIC would issue its first formal interpretation of the term “deposit liability” in Section 11(d)(11). Even if such an interpretation were found to be a change in the FDIC’s prior position, the Supreme Court has consistently upheld the authority of federal administrative agencies to modify their prior interpretations of statutes they are charged with administering, so long as the agency’s subsequent interpretation satisfies the “arbitrary and capricious” standard, as elaborated in Chevron, including by providing a reasoned basis for its interpretation. As the Supreme Court stated in Chevron: “An initial agency interpretation is not instantly carved in stone. On the contrary, the agency, to engage in informed rulemaking, must consider varying interpretations and the wisdom of its policy on a continuing basis.”⁶⁰ The court’s position in the Chevron case has been affirmed in more recent Supreme Court cases:

⁶⁰ Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837, 863–864 (1984).

“[I]f the agency adequately explains the reasons for a reversal of policy, ‘change is not invalidating, since the whole point of Chevron is to leave the discretion provided by the ambiguities of a statute with the implementing agency.’”⁶¹

We also note that revisions to the FDIC’s advisory opinions are not unprecedented.⁶²

VII. Related Considerations

- A. *The proposed interpretation would not increase potential losses to the FDIC even though the FDIC would theoretically share the assets of the failed bank with a larger group of claimants (both domestic and foreign uninsured depositors).*

As discussed above, the FDIC has recently concluded that the subordination of foreign branch deposits does not offer any significant benefits to the FDIC from a recovery perspective because, in the FDIC’s view, foreign branch deposits are likely to run off significantly prior to failure and, given the possibility of ring-fencing, are more like secured obligations.⁶³ Indeed, if the subordination of foreign branch deposits and local ring-fencing prevent the FDIC from being able to resolve a U.S. G-SIB on a “single entity” basis, the FDIC will be unable to preserve the going concern value of the global franchise and may even be unable to preserve fully the going concern value of the U.S. portion of the business. As a result, only the liquidation value of the U.S. business may be available to satisfy the claims of domestic depositors, including the FDIC’s claims as subrogee of insured depositors. Because the

⁶¹ Nat. Cable & Telecommunications Ass’n v. Brand X Internet Services, 545 U.S. 967, 981 (2005) (quoting Smiley v. Citibank (South Dakota), N.A., 517 U.S. 735, 742 (1996)). Compare Motor Veh. Mfrs. Ass’n v. State Farm Ins., 463 U.S. 29 (1983) (finding an agency had authority to overturn a previously promulgated standard, but the rescission at issue was “arbitrary and capricious” because the agency failed to present a reasoned basis for its decision to overturn the standard).

⁶² See, e.g., FDIC Advisory Opinion, Insurance of Public Unit Deposits, FDIC-85-7 (April 11, 1985) available at <http://www.fdic.gov/regulations/laws/rules/4000-1700.html> (“By an opinion letter of March 19, 1985, the Legal Division rescinded a 1979 opinion that had concluded that multiple custodians of public funds appointed pursuant to a Colorado statute were ‘official custodians’ for FDIC insurance purposes and entitled to separate deposit insurance.”).

⁶³ 76 Fed. Reg. 10672, 10681 (Feb. 25, 2011). See supra note 45 and accompanying discussion.

difference between a financial institution's going concern value and its liquidation value can be substantial, especially if failure occurs during a financial crisis,⁶⁴ the FDIC is likely to face greater (quite possibly, considerably greater) losses in a domestic "separate entity" resolution where foreign branch deposits are subordinate to domestic deposits than it would in a global "single entity" resolution where foreign branch deposits are *pari passu* with domestic deposits.

Therefore, the interpretation of "deposit liability" proposed in this Memorandum should not have any material adverse impact on the FDIC's recovery in a bank failure and could have a positive impact. Even if it did have an adverse impact to some extent, any possible decrease in the FDIC's recovery would obviously be far less detrimental to the DIF than making the deposits insurable. Moreover, under the current regime, sophisticated foreign parties concerned about subordination have strong incentives to take actions to insulate themselves from subordination (such as a secured financing rather than making a deposit). Indeed, some of these actions would, of necessity, go beyond attaining *pari passu* status and result in achieving a claim superior to that of the FDIC. As a result, these parties would have priority over the FDIC (and uninsured depositors) in liquidation. The proposal in this Memorandum would reduce the incentives to take such actions and thus would benefit the FDIC.

- B. *The prohibition in 12 U.S.C. § 1831r on federal banking agencies' taking action that has the effect of satisfying foreign branch deposits is not implicated.*

Section 1831r prohibits federal banking agencies from making any payment or providing any assistance, guarantee, or transfer in connection with any insured depository

⁶⁴ See, e.g., Douglas G. Baird & Edward R. Morrison, Dodd-Frank for Bankruptcy Lawyers, 28 (July 25, 2011) (Columbia Univ. Sch. Of Law Ctr. For Econ. Studies, Working Paper No. 401, 2011) available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1895692 (the "liquidation value" of a systemically important bank during an economic collapse "is likely to be close to zero"); Andrei Shleifer & Robert W. Vishny, Fire Sales in Finance and Macroeconomics, 25 J. Econ. Persp. 29 (2011).

institution which would have the direct or indirect effect of satisfying, in whole or in part, foreign branch deposits.⁶⁵

Section 1831r does not conflict with an interpretation of the term “deposit liability” in the DPR statute that includes foreign branch deposits. The DPR statute does not create a guarantee of federal support for “deposit liabilities” nor does it require payment of these deposits out of the DIF. Rather, Section 1831r is part of the “least cost resolution” legal framework that is separate and distinct from the DPR statute, which concerns itself only with priority. The definition proposed in this Memorandum would have no effect on Section 1831r or the class of deposits for which the FDIC is liable. In fact, one of its advantages is that it leaves foreign branch deposits out of the definition of “deposits” for deposit insurance purposes.

Indeed, the suggested approach is more consistent with the policy rationale underlying Section 1831r. In Section 1831r, Congress expressed an antipathy for federal monies being used to the benefit of foreign branch depositors. Given that banks’ only method to address subordination today, while preserving their branch structure, is to make those deposits payable in the United States, and thus insured, the amount of foreign branch deposits with deposit insurance will increase and thus the amount of federal monies that go to foreign branch depositors will also increase.

- C. *The proposed interpretation is consistent with 12 U.S.C. § 1823(c)(4)(E)(i)(II) which forbids use of insurance funds to protect “creditors other than depositors.”*

As part of the least cost resolution provisions in the FDIA, 12 U.S.C. § 1823(c)(4)(E)(i)(II) provides that the FDIC may not take any action, directly or indirectly, with respect to any insured depository institution that would have the effect of increasing losses to the DIF by protecting creditors other than depositors.

⁶⁵ 12 U.S.C. § 1831r.

Under the definition of “deposit liability” proposed in this Memorandum, “deposit liabilities” will include foreign branch deposits under the DPR statute but the definition will have no effect on the definition of “deposit” in Section 3(l)(5) and consequently no effect on the deposits or depositors that will receive funds out of the DIF in an insurance payout or otherwise. The proposed approach cleanly separates the treatment of foreign branch deposits for priority purposes under Section 11(d)(11) and for insurance purposes under Sections 3(l) and 3(m).

As a result, the interpretation proposed in this Memorandum would not be inconsistent with 12 U.S.C. § 1823(c)(4)(E)(i)(II) because the interpretation addresses only priority and will not involve an action by the FDIC that would increase losses to the DIF by protecting “creditors other than depositors”⁶⁶ or change the FDIC’s existing practices.⁶⁷ Moreover, as discussed above in Section VII.A, the proposed interpretation could actually be beneficial to the DIF, particularly given the FDIC’s conclusion that foreign depositor subordination does not provide any appreciable benefit to the DIF.

VIII. Alternative Regulatory Approaches

We understand that the FDIC has also considered other potential regulatory solutions to the policy concerns created by the DPR statute, as interpreted by the 1994 Advisory Opinion. We understand one of these potential solutions is an interpretation that (a) would afford deposits that are dually payable in both the United States and the host country “deposit liability” status under the DPR statute, but (b) would exclude them from the definition of “deposit” or would otherwise determine that they should not be “insured deposits.”

⁶⁶ The distinction between “depositors” and “creditors” in 12 U.S.C. § 1823(c)(4)(E)(i)(II) is consistent with the distinction we have proposed in this Memorandum in Section 11(d)(11) between “deposit liabilities” (which would include all depositors) and liabilities to general unsecured creditors.

⁶⁷ We recognize that the proposed interpretation, as well as any FDIC action that ends foreign branch deposit subordination, would theoretically increase the losses to general creditors that are not domestic or foreign branch depositors. This result, however, is consistent with clear Congressional intent in creating a preference for depositors.

Although a swift regulatory solution is preferable to no solution, we believe that this approach is significantly more complicated and tenuous than the approach we have proposed in this Memorandum. Any such approach is undesirable because it requires more complex interpretations touching multiple portions of the FDIA (at a minimum “deposit” under Section 3(l), “deposit liability” under Section 11(d)(11) and “insured deposit” under Section 3(m)). Furthermore, it may be more challenging for the FDIC to argue that dual payable deposits may be “deposits” for priority purposes but not for insurance purposes given the long-standing equivalence provided for “deposit” and “insured deposit” based on the close relationship between their definitions in Section 3(l) and Section 3(m), respectively. Unlike the term “deposit liability” in the DPR statute, the alternative approach does not appear to involve the interpretation of terms that the FDIC could argue are clearly ambiguous. Indeed, such an interpretation would seem to require reading language into the existing text of the definitions in the FDIA that Congress has already provided. As a result of the above considerations, an alternative approach may be more difficult to defend on a legal basis, if challenged.

Moreover, because the interpretations required in the alternative approach touch such basic and ubiquitous terms as “deposit” and “insured deposit,” the alternative approach may necessitate further interpretations, by the FDIC or other federal banking agencies, to cure any unintended consequences. For example, supporting bank action to create dually payable deposits would undermine the U.S. public policy interest in requiring foreign branch depositors to bear the sovereign risk of the country in which the foreign branches are located, such as the risk of asset freezes or expropriations.⁶⁸

Any approach that relies on dual payability also presents many unnecessary implementation concerns. Rather than accomplishing the solution cleanly through regulatory

⁶⁸ This public policy is reflected in Section 25C of the Federal Reserve Act. See supra note 46.

action, this approach would first require banks to restructure customer relationships and to make foreign branch deposits dually payable. For example, banks would need to modify the contracts of all their foreign branch customers, and (depending upon the institution and the individual contractual requirements) may need to obtain customer consent. Furthermore, in addressing this issue with customers, the concept of employing dual payability to address an esoteric issue in U.S. law is likely to cause customer confusion, and worse, a potential loss of customers over such confusion, or over other unrelated matters such as tax, jurisdictional or contractual issues.

An interpretation adopted in a regulation providing that deposits payable both in the U.S. and in a foreign jurisdiction will not be insured creates substantially greater interpretative, consistency and practical questions than the simpler regulatory interpretation of the undefined term “deposit liability” in the DPR statute that we have proposed in this Memorandum. We submit, therefore, that the FDIC should choose the simpler route proposed in this Memorandum and formally define “deposit liability” under Section 11(d)(11) as inclusive of foreign branch deposits.

IX. Conclusion

Recent developments have made it clear that the FDIC and banks have a strong policy interest in concluding that foreign branch deposits are not subordinated to domestic deposits under the DPR statute without requiring that those deposits become insured deposits. Indeed, based on developments in the market and the increased need to address cross-border regulatory issues since the early 1990s, prompt actions to address the concerns created by foreign branch depositor subordination has become essential.

Not only does an interpretation of “deposit liability” in Section 11(d)(11) to include foreign branch deposits, as proposed in this Memorandum, achieve this goal, but, we also believe that it is the most appropriate interpretation of the term. The plain meaning of the term,

its use in other portions of the FDIA, the legislative history of the FDIA and the analogous state law provisions all point to this conclusion. This definition would prevent the negative consequences to the FDIC and to banks discussed above and would further international cooperation in multinational bank resolutions. Furthermore, our proposed approach accomplishes these objectives with the interpretation of a single undefined term in the FDIA. Given the recent developments and the policy considerations discussed above, the FDIC would have a more than sufficient basis to issue its first formal interpretation of the term, notwithstanding the 1994 Advisory Opinion.

Given the different interpretation in the 1994 Advisory Opinion, the FDIC could also take the position that the term “deposit liability” is susceptible to more than one interpretation and is thus ambiguous. The FDIC is clearly authorized to resolve such an ambiguity by adopting the interpretation proposed in this Memorandum because it is a reasonable construction of the term and advances the FDIC’s policy interests. A reviewing court, therefore, would grant the FDIC Chevron deference in reviewing such an interpretation.

Cleary Gottlieb Steen & Hamilton LLP

Davis Polk & Wardwell LLP

Sullivan & Cromwell LLP

Appendix B

Law Firm Memo Supplement

STATUS OF FOREIGN BRANCH DEPOSITS

ALTERNATIVE APPROACH

February 4, 2013

Introduction

This Memorandum supplements our Memorandum of January 2, 2013 (the “Joint Memorandum”) and describes an approach that our three firms believe accommodates the multiple concerns potentially raised by Sections 11(d)(11)¹ and 3(m)² of the Federal Deposit Insurance Act (the “FDIA”) with respect to foreign branch deposits.

As stated in the Joint Memorandum, we believe that the potential or actual subordination of foreign branch deposits would have profound adverse consequences. These consequences would include: creating an obstacle to international regulatory cooperation, encouraging nationalistic ring-fencing and impeding resolution of multinational banks.

We also believe that it is not necessary to make foreign branch deposits insured in order to avoid these adverse consequences. Rather, it is only necessary that foreign branch deposits be *pari passu* with domestic deposits in the liquidation of a failed bank. Moreover, we believe that an approach of avoiding subordination of foreign branch deposits by making them dually payable, both at the location of the foreign branch and at an office of the bank in the United States, has its own significant adverse consequences for the FDIC, as well as for banks. As outlined in the Joint Memorandum, and below, these consequences include likely elimination of the protections of Section 25C of the Federal Reserve Act,³ increased reserve requirements,

¹ 12 U.S.C. § 1821(d)(11).

² 12 U.S.C. § 1813(m).

³ 12 U.S.C. § 633.

administrative and financial burdens of implementation and foreign regulatory scrutiny that it has been properly implemented, as well as additional claims on the DIF.

Accordingly, if the FDIC determines that foreign branch deposits are not subordinated, there will then be no significant customer demand, or host country regulatory pressure, to develop dually-payable foreign branch deposits entitled to FDIC insurance. Indeed, banks will have significant disincentives to move towards dual-payability.

The question, therefore, is how best to accommodate the concerns about both subordination and dual-payability in resolving the status of foreign branch deposits.

The Joint Memorandum, we believe, presented a simple and direct way of dealing effectively with both these issues. An interpretation of “deposit liability” in Section 11(d)(11) as including foreign branch deposits would eliminate both the subordination of foreign branch deposits and any new incentives for host jurisdictions or banks to make foreign branch deposits dually-payable.⁴

Nonetheless, if the FDIC would still be concerned about the risk of dual-payability to the Deposit Insurance Fund (the “DIF”) and becoming “insurer to the world”, we have developed an alternative hybrid approach, which, as described in this supplemental Memorandum, would also accomplish these objectives from both a legal and policy perspective.

For any approach to be effective, however, there must be either a formal interpretation or rulemaking by the FDIC (each, an “FDIC Action”).

⁴ Banks have long had the ability under the FDIA to make their foreign branch deposits insured by making them dually payable. Yet, to this date, we are not aware of any move towards dual-payability or of any desire by banks, or significant demands by customers, to do so. Indeed, in a recent comment letter by the American Bankers Association Securities Association to the U.K. Financial Services Authority regarding its Consultation Paper on depositor preference regimes, the members—consisting of the U.S. banks with the vast majority of foreign branch deposits—stated that they prefer a solution that does not require change to the customer relationship or change to the bank’s operational structure. Yet, banks realize that, without some legislative or regulatory action outside their control, they may have to address the issue in the only way that can be effected by the banks themselves—by employing dual-payability. Removing the need to employ such a solution would eliminate the most significant incentive for banks to create dually-payable deposits.

Two Possible Approaches: Dual-Interpretation Approach and Alternative Approach

We understand that one approach the FDIC may be considering involves two interpretations of dually-payable foreign branch deposits (referred to herein as the “Dual-Interpretation Approach”). Under this approach: (i) dually-payable foreign branch deposits would be interpreted to constitute a “deposit liability” under Section 11(d)(11), and, therefore, would not be subordinated to domestic deposits in a liquidation; but (ii) dually-payable foreign branch deposits would be interpreted not to constitute a “deposit” for purposes of Section 3(l), as incorporated into the definition of “insured deposit” under Section 3(m), and, therefore, would not be insured. Either implicitly or explicitly in the Dual-Interpretation Approach, foreign branch deposits that are not dually payable (i.e., that are payable only at the foreign branch) would be interpreted not to constitute a “deposit liability” for purposes of Section 11(d)(11), and, therefore, would be subordinated to domestic deposits in a liquidation.

We respectfully submit that, as noted above, the solution recommended in our Joint Memorandum resolves the legal and policy issues related to the status of foreign branch deposits more effectively, without any need for the FDIC to take additional action to interpret the insured status of dually-payable foreign branch deposits. However, if the FDIC believes that it is necessary to deal with the “insurer to the world” issue by eliminating deposit insurance for dually-payable deposits, we believe there is a better approach than the Dual-Interpretation Approach that would fully accommodate and, indeed, enhance the FDIC’s protection against becoming insurer to the world. Under this alternative approach (the “Alternative Approach”), the FDIC would (i) interpret the term “deposit liability” in Section 11(d)(11) of the FDIA to include foreign branch deposits (without requiring dual-payability); and (ii) interpret the term “deposit” in Section 3(l) to exclude foreign branch deposits, unless they are payable solely in the United States. An alternative to the latter interpretation to address the FDIC’s concerns could be

to provide some calibrated further disincentive to banks using dually-payable deposits, such as expressly considering the amount of such deposits for FDIC assessment purposes. An approach providing for disincentives rather than exclusion would be on more solid legal footing.

We submit that the Alternative Approach (i) is far more sustainable on a legal basis than the Dual-Interpretation Approach; (ii) creates considerably less risk to the DIF than the Dual-Interpretation Approach; and (iii) creates considerably less risk to the U.S. banking system than the Dual-Interpretation Approach.

Legal Analysis

The Dual-Interpretation Approach would require the FDIC to treat dually-payable foreign branch deposits in different and contradictory ways. For purposes of Section 3(l), as incorporated in Section 3(m), they would be *excluded* from “deposit” and “insured deposit”, but for purposes of Section 11(d)(11), they would be *included* as a “deposit liability”. As explained below, such an approach creates significant internal confusion within the FDIA, necessarily leads to logical inconsistencies and appears to violate basic canons of statutory construction. Because there is no clear statutory basis for applying the same term inconsistently, such an approach would be subject to substantial risk of judicial rejection. Although an FDIC Action would normally be entitled to judicial deference, we believe that the direct inconsistency in the Dual-Interpretation Approach would diminish, and quite possibly eliminate, that deference.

A fundamental legal assumption underlying the Dual-Interpretation Approach must be that foreign branch deposits do not constitute a “deposit liability” under Section 11(d)(11) unless they are dually payable.⁵ This legal assumption is apparently based on the premise that “deposit liability” in Section 11(d)(11) has the same meaning as “deposit” in

⁵ If all foreign branch deposits were per se a deposit liability, as we have proposed in the Joint Memorandum, it would make no difference whether the deposit were dually payable. This further underlines our position that under the approach proposed in the Joint Memorandum, the risk of banks moving towards dual-payability and the FDIC becoming “insurer to the world” is remote.

Section 3(l), including the “carve out” for foreign branch deposits in Section 3(l)(5)(A).⁶

Therefore, foreign branch deposits would be excluded from being a deposit liability by Section 3(l)(5)(A), as incorporated into Section 11(d)(11), unless the deposits were included by Section 3(l)(5)(A)(ii) because they are dually payable.

But this fundamental legal assumption conflicts directly with the other key aspect of the Dual-Interpretation Approach that is designed to deal with the “insurer to the world” concept. It undermines the FDIC’s ability to argue that Section 3(l)(5)(A)(ii) does not produce the exact same result with respect to dually-payable deposits when the Section 3(l) definition of “deposit” is incorporated into the definition of “insured deposit” in Section 3(m). In other words, if the Dual-Interpretation Approach were adopted, the FDIC would be forced to argue that Section 3(l)(5)(A)(ii) is interpreted differently when it is incorporated into Section 3(m) than when incorporated into Section 11(d)(11). We are aware of no basis for that argument.

In contrast, the Alternative Approach does not create this dilemma because dually-payable deposits would need to be interpreted for only one section of the FDIA, that is, Section 3(l), which interpretation would be incorporated into the definition of “insured deposit” in Section 3(m). Under the Alternative Approach, the subordination issue would be dealt with without reliance on dual-payability because all foreign branch deposits are entitled to be treated equally with all other deposits as a “deposit liability” for purposes of Section 11(d)(11).⁷ This avoids the inherent inconsistency of the Dual-Interpretation Approach. In other words, the Dual-Interpretation Approach requires that, in effect, the same term be applied differently in

⁶ This appears to be consistent with the view taken in a 1994 advisory opinion by the then Acting General Counsel of the FDIC (the “1994 Advisory Opinion”). FDIC Advisory Opinion, “Deposit Liability” for Purposes of National Depositor Preference Includes Only Deposits Payable in U.S., FDIC 94-1 (February 28, 1994). As pointed out in the Joint Memorandum, the 1994 Advisory Opinion has never been codified or otherwise formalized, and the FDIC has apparently never faced a situation where it was required to take any action based on the 1994 Advisory Opinion.

⁷ Although the FDIC has the general authority to interpret the FDIA, it is important to note, for purposes of the Alternative Approach, that the FDIC has separate and independent authority under Section 11(d)(1) to interpret Section 11(d)(11) of the FDIA without needing to link such an interpretation to determinations made with respect to Section 3(l) or under Section 3(l)(5). See 12 U.S.C. § 1821(d)(1).

separate sections, which violates basic canons of statutory construction, whereas the Alternative Approach requires that different terms be applied differently in separate sections, which is required by those same canons.

A potential attraction of the Dual-Interpretation Approach is that it may appear to avoid inconsistency with the interpretation of Section 11(d)(11) in the 1994 Advisory Opinion. In fact, however, the Dual-Interpretation Approach creates its own inconsistency with the 1994 Advisory Opinion. That Advisory Opinion and its underlying premise (i.e., that the definitions of “deposit” and “deposit liability” are coterminous) implicitly require the conclusion that, under Section 3(l)(5)(A), once a deposit is “payable in the United States”, it must be a “deposit” for all purposes in the FDIA, including for purposes of deposit insurance and for purposes of the meaning of “deposit liability”. Because the Dual-Interpretation Approach provides that dually-payable foreign branch deposits are both not subordinated and are not insured, adoption of the Dual-Interpretation Approach would be inconsistent with the premise of the 1994 Advisory Opinion.

Moreover, for the reasons set forth in the Joint Memorandum, we continue to believe strongly that, contrary to the 1994 Advisory Opinion, the term “deposit liability” as used in Section 11(d)(11) includes, and therefore does not subordinate, deposits of foreign branches of U.S. banks. Accordingly, it is not necessary to make those deposits dually payable in order to escape subordination. This legal position is supplemented by equally strong policy considerations, including risk to the DIF, as outlined in the Joint Memorandum.

Risks Posed by the Dual-Interpretation Approach

Risks to the FDIC.

We believe that that Dual-Interpretation Approach exposes the DIF to major additional claims, and ultimately losses, in the event that it is challenged and overturned in the courts.

Perhaps the greatest risk is that the FDIC Action adopting the Dual-Interpretation Approach is overturned in the context of the future failure of a large international bank. In the event of such a failure, the likelihood of a claim that dually-payable deposits are insured is close to inevitable. There would be a large class of economically-motivated plaintiffs, and some would undoubtedly seek to challenge the FDIC Action in order to obtain full FDIC insurance. If they are successful, the DIF could potentially encounter losses of many billions of dollars, representing a substantial portion of the DIF's total resources.

Even if the judicial challenge is initiated shortly after an FDIC Action adopting the Dual-Interpretation Approach, the success of that judicial challenge could expose the FDIC to huge additional claims. Once such an FDIC Action is taken, and even when it is initially proposed, there will be an immediate movement of foreign branch deposits to dually-payable status. If a court subsequently overturned the FDIC Action, it would be too late to “un-ring the bell” on the migration of foreign branch deposits to dual-payability. There will be substantial incentives for foreign branch depositors to retain their dually-payable status, both to obtain insurance and, even more so, to ensure against subordination.

This very substantial risk to the DIF under the Dual-Interpretation Approach is significantly lowered by the Alternative Approach. Under the Alternative Approach, there will be no foreign branch depositor rush to make their deposits dually-payable and the Alternative

Approach is on firmer legal ground because it does not treat the relevant statutory terms in the FDIA inconsistently.⁸

Moreover, even if a court agreed with the Dual-Interpretation Approach to the extent that dual-payability does not affect the uninsured status of foreign branch deposits, it could seek to provide statutory consistency by also finding that dually-payable foreign branch deposits remain subordinated. Such a decision would leave the FDIC with legislation as the only resort to resolve the subordination of foreign branch deposits. In other words, the result of an immediate judicial challenge to a Dual-Interpretation Approach could be “heads you lose; tails you lose”.

In a challenge to the Alternative Approach, a court could also find either that dually-payable foreign branch deposits are insured or that all foreign branch deposits are subordinated, but the consequences are far less severe. In the event of the former decision, because the FDIC will have issued an interpretation that (i) dual-payability is not required to cure subordination under Section 11(d)(11) and (ii) dually-payable foreign branch deposits are not insured, it would be extremely unlikely for customers or banks to have moved to dual-payability, and, thus, the additional exposure of the DIF would, as a practical matter, be negligible. In the event of the latter decision, the FDIC would still have the ability to try to address the subordination issue through a regulatory approach, such as the Dual-Interpretation Approach.

We recognize one other possible litigation concern with adopting the Alternative Approach is, potentially, that, in the event of a failure, uninsured domestic depositors would sue the FDIC on the basis that they were entitled to priority over foreign branch depositors. We submit that this risk is considerably less than the risks to the FDIC and the DIF under the Dual-Interpretation Approach, both because of the relative legal merits of the two approaches and

⁸ Even this limited risk would be eliminated if the FDIC adopted the original proposal set forth in the Joint Memorandum. In that case, there would not be any need for FDIC Action to address the insurance status of dually-payable deposits.

because such a claim would be against the receivership estate of the failed bank, rather than the DIF.⁹ Moreover, the converse risk must also exist. If the Alternative Approach were not adopted, foreign branch depositors that were not dually payable could claim that the FDIC improperly subordinated their claims.

Although the focus in this Memorandum is on risk to the DIF, the ultimate risk is, of course, borne by the U.S. banking system. A multi-billion dollar successful claim on the DIF would be highly damaging to all U.S. banks, including small banks. All banks would be subject, on a relative basis, to a massive assessment to restore the DIF to appropriate levels.

Risks to the U.S. Banking System.

The Dual-Interpretation Approach could expose U.S. banks with foreign branches to substantial additional risk, because it could strip them of the protection afforded by Congress in Section 25C of the Federal Reserve Act.

Section 25C provides that a bank is not required to repay foreign branch deposits at its offices in the United States if foreign government expropriation or *force majeure* prevents payment of those deposits at the foreign branch, unless the bank has expressly agreed in writing to repay the deposit “under those circumstances”. In enacting Section 25C in 1994, Congress intended to overturn then-recent Court of Appeals decisions that had concluded that a home office was responsible for the liabilities of its branches and was required to repay foreign branch depositors at the home office, even if the underlying assets in the foreign branch supporting the deposits were seized or were otherwise unavailable to the bank.

The Dual-Interpretation Approach would have the effect of overturning Congress’ decision and creating very substantial risk for banks. Depending on how a Court interpreted

⁹ A litigation risk may also exist with respect to claims by general creditors that foreign branch depositors should have been *pari passu* with, rather than superior to, the general creditors. In addition to the reasons that uninsured domestic depositors are unlikely to sue, given that general creditors already have a very low expectation for recovery and expect to be subordinated to depositors, we believe this risk of litigation by general creditors is even more remote.

Section 25C, potentially multiple U.S. banks could be placed at risk of significant losses. In today's world, with increasing global ring-fencing, we may need to be concerned about more than revolutionary expropriations, as occurred, for example, in the past in Cuba and Vietnam. Expropriation, in practice or in effect, could arise in a major developed country.

Although potentially of less importance than the Section 25C exposure in relative terms, the Dual-Interpretation Approach creates other immediate risks to the banking system that are of significance in absolute terms. First, under the Dual-Interpretation Approach, banks would be required to hold reserves against their foreign branch deposits, which are otherwise exempt from reserve requirements. Although this is the banks' direct problem, the DIF is placed at greater risk if the earnings capacity of banks is weakened.

Second, the Dual-Interpretation Approach would require U.S. banks to engage in an administratively challenging restructuring of their foreign branch deposit agreements, as well as make unnecessary operational and technological changes to implement a dual-payability regime. The process of repapering deposit agreements will at a minimum create confusion and concern in the marketplace and will also require substantial due diligence scrutiny by foreign regulators in order for them to be satisfied that it will work as a practical matter. Given the complexity and inconsistencies associated with the Dual-Interpretation Approach, we believe that the FDIC Action itself could be a source of potential market, customer and foreign regulator confusion. This could result in a potential loss of foreign branch deposits without solving the foreign ring-fencing or subsidiarization risk. Banks also have indicated that in order to implement dual-payability on a broad scale, significant modifications to internal systems would be required, for example, to separately identify time and demand foreign branch deposits (for purposes of reserve requirements), to implement protections against double payment of deposit

or, in the event of failure, double deposit insurance (in the U.S. and the host country) and to address payment of deposits in multiple currencies.

Conclusion

The intended effect of both the Dual-Interpretation Approach and the Alternative Approach on foreign branch deposits is basically the same. Under either approach, foreign branch deposits would be uninsured but on a parity with domestic deposits in a liquidation.

There is, however a substantial difference in the potential actual effect, which arises principally from the relative legal risks of judicial rejection and attendant monetary and non-monetary consequences to the FDIC and to U.S. banks. We respectfully submit that the Alternative Approach (as well as the approach described in the Joint Memorandum) is significantly more likely to withstand legal challenge than the Dual-Interpretation Approach and, even if successfully challenged, would result in significantly less adverse consequences. In addition, the Dual-Interpretation Approach creates greater exposure and earnings pressure for U.S. banks. We, therefore, urge the FDIC to adopt either the approach proposed in the Joint Memorandum or the Alternative Approach to resolve the status of foreign branch deposits under the FDIA.

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Appendix C

Required Clarifications for Regulatory Reporting Purposes

Banks will require significant and detailed guidance with regard to various regulatory reports in order to fully implement the effective requirement to adopt dually payable deposits in order to resolve the subordination of foreign depositors. Guidance from the FDIC (and potentially the other Federal regulators) will have to be comprehensive and consistent across the various reports. In addition, such guidance will have to recognize the potential additional ramifications and policy impacts that changes in these reports will have.

The main question for most of these issues is whether dually payable deposits are to be treated as foreign, domestic, or potentially both. Coming to a conclusion on this point is complicated by a number of factors:

- The definition of “deposits” in the Glossary related to the “Instructions for Preparation of Consolidated Reports of Condition and Income (FFIEC 031 and 041)” (March 2013) includes a discussion of the definition in FDIA § 3(1), yet it states that “for purposes of these reports, the reporting standards for deposits specified in these instructions do not strictly follow the precise legal definitions . . .”
- The fact that the definition of “deposits” in the FFIEC 031 Glossary describes the FDIA definition would seem to imply that, perhaps, foreign deposits that are not dually payable in a U.S. office would not be included in the term deposits at all for purposes of the FFIEC 031 Report (or “Call Reports”). However, this cannot be the case, as a number of the reports include foreign deposits (*see, e.g.*, Schedule RC-E Part I (“deposit liabilities of the domestic offices of the consolidated bank”) as compared to Schedule RC-E Part II (“deposit liabilities of the foreign offices . . . of the consolidated bank”);¹ Schedule RC-O, Item 1 (“ . . . gross total deposit liabilities are the combination of: All deposits in ‘domestic offices’ reported in Schedule RC, item 13.a; All deposits in ‘foreign offices’ reported in Schedule RC, item 13.b, on the FFIEC 031 report; . . .”).
- Exacerbating the issue is the fact that the Call Reports use various formulations, without specific definitions, of “domestic deposits”, “foreign deposits”, “deposits in domestic offices”, “deposits in foreign offices,” “deposit liabilities of domestic offices,” and “deposit liabilities of foreign offices,” among others.
- The preamble to the Proposal states that, in the past, a dually payable deposit “increased a bank’s deposit insurance assessment base (which, in the past, excluded deposits solely payable outside the United States) and, thus, its deposit insurance assessment.”² Prior to the changes under the Dodd-Frank Act, the deposit insurance

¹ We note that at least the first page of the instructions for Schedule RC-E uses the term “deposit liabilities”, seemingly to indicate the broader term that would encompass foreign deposits, rather than formulations that narrow the term “deposits” by excluding foreign deposits that are not dually payable. This is further support for adoption of the combined approach that we support in this letter.

² 78 Fed. Reg. at 11,605.

assessment base, with some modifications, was based on Call Report line items that included “domestic deposits.” Therefore, the preamble implies that the FDIC believes that a dually payable deposit becomes a domestic deposit.

- However, FDIA § 3(l)(5)(A), as well as the Proposal’s change to 12 C.F.R. § 330.3(e)(2), state that a dually payable deposit would seem to remain as a deposit “carried on the books and records of an office of such institution located outside the States of the United States . . .”³

Therefore, the industry is in need of guidance on how dually payable deposits should be reported. This is not a minor administrative issue, however. Changes to the Call Reports carry potentially significant changes to internal systems (particularly, if different reports may treat the deposits differently), and as mentioned below certain issues with broader ramifications arise.

A. Required Clarifications to Operationalize Dually Payable Deposits in Regulatory Reporting Systems

Below, we list several items from the Call Reports and other regulatory reports for which clarification of the appropriate method of including dually payable deposits would be necessary:

- FFIEC 009—Country Exposure Report. Would “conditional payment” (see Section V.C. of the accompanying letter) cause dually payable deposits to continue to be included in foreign office “local liabilities”?
- FFIEC 030—Foreign Branch Report of Condition.
- FFIEC 031—Consolidated Reports of Condition and Income
 - Schedule RI—Income Statement. Particularly in relation to interest expense and service charge income.
 - Schedule RC—Balance Sheet.
 - Schedule RC-E—Deposit Liabilities.
 - Schedule RC-H—Selected Balance Sheet Items for Domestic Offices. In addition to appropriate reportable item, guidance would be needed on the impact, if any, on net due from/to foreign offices.
 - Schedule RC-K—Quarterly Averages.
- FR 2502q—Foreign Branch Reports
- FR Y-9C—Consolidated Financial Statements for Holding Companies.

³ 78 Fed. Reg. at 11,609. The language in FDIA § 3(l)(5)(A) is similar, but not exactly the same: “carried on the books and records of an office of such bank or savings association located outside any State . . .”

- TIC (Treasury International Capital System) Reports. What, if any, changes result from the introduction of dually payable deposits?

B. Certain Clarifications that Have Broader Ramifications

Below we describe a few examples where the appropriate reporting of dually payable deposits is likely to have significant ramifications:

- FDIC Summary of Deposits. This summary is used to determine depository institution market share. Including or not including foreign dually payable deposits could have a significant impact on competitive standing, as the publication of this report often garners much attention. In addition, there could be knock-on effects in relation to mergers and acquisitions and other analyses dependent upon geographic market share.
- FR 2644—Weekly Report of Selected Assets and Liabilities of Domestically Chartered Commercial Banks and U.S. Branches and Agencies of Foreign Banks. As the Federal Reserve Board indicates on its website: “Data from this report are used in conjunction with other data to construct estimates of bank credit, sources and uses of bank funds, and a balance sheet for the entire banking system. These statistics are used to analyze current banking and monetary conditions.” Information on this report feeds into decisions regarding U.S. monetary policy.
- Core Deposits: Under the FDIC’s final large bank assessment rule,⁴ core deposits form an integral part of the analysis of a bank’s ability to withstand funding related stress. There is no clear definition of “core deposits” in the rule, but in Appendix A to Subpart A of Part 327 of the FDIC’s rules, in the “Description of Scorecard Measures,” the “Core Deposit/Total Liabilities” ratio is described as “Total domestic deposits excluding brokered deposits and uninsured non-brokered time deposits divided by total liabilities.” We understand that, when calculating this ratio the formula currently in use is: (a) Domestic deposits from Schedule RC, item 13.a, minus (b) total brokered deposits from Schedule RC-E, memo item 1.b., minus (c) non-brokered time deposits of more than \$250,000 (in domestic offices) from Schedule RC-O, memo item 12.

Notwithstanding this currently used formula, there is significant evidence that dually payable deposits should be treated as core deposits. Pursuant to Schedule RC-O, which we understand is used as additional information related to deposit insurance assessments, “foreign deposits” for purposes of items 2 and 3 are defined with reference to the exclusion from the definition of “deposits” in FDIA § 3(l)(5)(A). Based on that definition, “foreign deposits” do not include those deposits that provide for “payment at an office of the depository institution located in any State.” Therefore, dually payable deposits are not “foreign deposits” as used for insurance assessment purposes, should be deemed “domestic deposits” for such purposes, and should be deemed “core deposits” for purposes of the FDIC’s assessment rules.

⁴ FDIC, “Assessments, Large Bank Pricing,” 76 Fed. Reg 10,672 (Feb. 25, 2011).

C. The Need for Additional Consistent Guidelines and Interpretations in Connection with Regulatory Reporting Matters

In addition to the technical reporting form items noted above, there is further need for clarity on a number of broader questions and issues:

- Any guidance must be carefully crafted so as to be consistent across all reports. In particular, any formulae for interseries comparisons and between reports would need to be reviewed and revised as necessary.
- Product characteristics of deposit accounts in foreign branches may be very different from those in U.S. accounts. U.S. banks will be reviewed on their product determinations during examinations related to required reserves. Guidance will be needed for banks and examiners on how to analyze dually payable deposits for purposes of product distinctions relevant to Regulation D (*i.e.*, demand, time, transaction, non-transaction, etc.)
- In examinations related to required reserves and (in the past) related to insurance assessments, regulators have required customer-level data with regard to certain deposits. Dually payable deposits should be “core deposits” for assessment purposes and will be subject to Regulation D reserve requirements, although they will be deposits originating from foreign offices. Foreign depositors are likely to be subject to local privacy and data protection rules that are different from those in the United States, and examiners will have to be made aware that certain customer-level data may not be able to be provided.
- Local jurisdiction accounting may impact what is treated as a deposit in foreign branches and what is not. Guidance will be necessary on addressing differences in foreign accounting practices.