

UNITED STATES: FINANCIAL SECTOR ASSESSMENT
PROGRAM - REVIEW OF THE KEY ATTRIBUTES OF
EFFECTIVE RESOLUTION REGIMES FOR THE
BANKING AND INSURANCE SECTORS—TECHNICAL
NOTE



UNITED STATES

FINANCIAL SECTOR ASSESSMENT PROGRAM

July 2015

REVIEW OF THE KEY ATTRIBUTES OF EFFECTIVE RESOLUTION REGIMES FOR THE BANKING AND INSURANCE SECTORS—TECHNICAL NOTE

This Technical Note on the Review of the Key Attributes of Effective Resolution Regimes for the Banking and Insurance Sectors on the United States was prepared by a staff team of the International Monetary Fund. It is based on the information available at the time it was completed in June 2015.

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TECHNICAL NOTE

REVIEW OF THE KEY ATTRIBUTES OF EFFECTIVE RESOLUTION REGIMES FOR THE BANKING AND INSURANCE SECTORS

Prepared By
**Monetary and Capital
Markets Department and
Legal Department**

This Technical Note was prepared in the context of an IMF Financial Sector Assessment Program (FSAP) mission to the United States of America, led by Aditya Narain and overseen by the Monetary and Capital Markets Department, IMF. Further information on the FSAP program can be found at <http://www.imf.org/external/np/fsap/fssa.aspx>

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Glossary

| | |
|--------|---|
| ABS | Asset Backed Securities |
| AIG | American International Group |
| AM | Assessment Methodology |
| BCP | Basel Core Principles for Effective Bank Supervision |
| BHC | Bank Holding Company |
| CCP | Central Counterparty |
| CFPB | Consumer Financial Protection Bureau |
| CFR | Code of Federal Regulations |
| CFTC | Commodity Futures Trading Commission |
| CMG | Crisis Management Group |
| CME | Chicago Mercantile Exchange |
| COAG | Cooperation Agreement |
| CP | Core Principle |
| DIF | Deposit Insurance Fund |
| DFA | Dodd-Frank Wall Street Reform and Consumer Protection Act |
| EC | Essential Criteria |
| EN | Explanatory Note |
| FBA | Federal Banking Agency |
| FBO | Foreign Bank Organization |
| FDI | Federal Deposit Insurance |
| FDIC | Federal Deposit Insurance Corporation |
| FIO | Federal Insurance Office |
| FMI | Financial Market Infrastructure |
| F.R. | Federal Register |
| FRB | Federal Reserve Board |
| FSAP | Financial Sector Assessment Program |
| FSB | Financial Stability Board |
| FSOC | Financial Stability Oversight Council |
| FTCA | Federal Tort Claims Act |
| GA | Guaranty Association |
| GDP | Gross Domestic Product |
| GF | Guaranty Fund |
| GSE | Government-Sponsored Enterprises |
| G-SIB | Global Systemically Important Banks |
| G-SIFI | Global Systemically Important Financial Institutions |
| G-SII | Global Systemically Important Insurers |
| IAIG | Internationally Active Insurance Group |
| IBA | International Banking Act |
| IDI | Insured Depository Institution |
| IHC | Intermediate Holding Company |
| IHCA | Insurance Holding Company System Regulatory Act |
| IMF | International Monetary Fund |
| IOSCO | International Organization of Securities Commissions |

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| | |
|-----------|---|
| IRMA | Insurer Receivership Model Act |
| ISDA | International Swaps and Derivatives Association |
| KA | Key Attributes of Effective Resolution Regimes for Financial Institutions |
| LBO | Large Banking Organizations |
| MDL | Model Act |
| MPE | Multiple Point of Entry |
| NAIC | National Association of Insurance Commissioners |
| NBFC | Nonbank Financial Company |
| NCUA | National Credit Union Association |
| NCUSIF | National Credit Union Share Insurance Fund |
| NOHLGA | National Organization of Life and Health Insurance Guaranty Associations |
| NY | New York |
| OCC | Office of the Comptroller of the Currency |
| OFR | Office of Financial Research |
| OLA | Orderly Liquidation Authority |
| OLF | Orderly Liquidation Fund |
| P&C | Property and Casualty Insurance |
| PCA | Prompt Corrective Action |
| PFMI | CPSS-IOSCO Principles for Financial Market Infrastructures |
| PWG | President's Working Group on Financial Markets |
| QFC | Qualified Financial Contract |
| RBC | Risk Based Capital |
| RMS | Risk Management Supervision |
| RRP | Recovery and Resolution Plans |
| SEC | Securities and Exchange Commission |
| SIPA | Securities and Investor Protection Act |
| SIPC | Securities Investor Protection Corporation |
| SLHC | Savings and Loans Holding Companies |
| SPE | Single Point of Entry |
| SR | Supervision and Regulation |
| TLAC | Total Loss Absorbing Capital |
| U.S. | United States |
| USC | United States Code |
| U.S. GAAP | United States Generally Accepted Accounting Principles |

EXECUTIVE SUMMARY AND KEY FINDINGS

The United States’ resolution regime for financial institutions has been significantly enhanced since the financial crisis. The Orderly Liquidation Authority (OLA), introduced in 2010 as part of the Dodd-Frank Act (DFA), provides the authorities with a robust framework for facilitating the resolution of most financial institutions that have the potential to cause severe systemic disruption and/or expose taxpayers to loss in the event of their failure. In particular, OLA is intended as a credible alternative to, and a substitute for, ordinary bankruptcy proceedings that can be disruptive from a financial stability perspective.

Over the past several years, the U.S. authorities have undertaken significant efforts to develop the capability to deploy the OLA, if and when needed, to safeguard financial stability. Of particular importance is the development of the so-called single point of entry (SPE) strategy, designed to take advantage of most systemically important financial institutions in the United States being organized under a holding company structure. Under the SPE strategy, the FDIC would resolve the financial group by initiating an OLA receivership at the holding company level. The strategy allows for a recapitalization of the group, with the shareholders and creditors of the failed holding company absorbing its losses. The SPE strategy’s key benefit lies in the avoidance of the need for separate resolution proceedings for the group’s operating companies (e.g., insured depository institutions (IDIs), insurance companies), which would otherwise add significant complexities. While the OLA provides the FDIC with flexibility to also apply alternative MPE resolution strategies, the benefits of SPE may, in many circumstances, make it more advantageous. The feasibility of an SPE strategy hinges on a number of factors, including the sufficiency of ‘bail-inable’ debt at the level of the holding company and internally within the group. This precondition to an SPE strategy may prove difficult for complex insurance groups; as such, an MPE may be the more appropriate strategy for insurance companies in some circumstances. Furthermore, reforms to address structural and organizational impediments to orderly resolution are required.

With respect to the banking sector, the resolution regime as set out in OLA and the Federal Deposit Insurance (FDI) Act is in broad conformity with the Financial Stability Board’s (FSB) Key Attributes of Effective Resolution Regimes for Financial Institutions (KA). The regime lays out a comprehensive framework through which the FDIC, through an administrative process, can exercise a broad range of resolution powers to deal with a failing systemically important bank or bank holding company (BHC), while protecting financial stability. The regime reflects the deep-rooted experience of the FDIC in dealing with distressed banks—experience that has placed the U.S. authorities at the forefront of international policymaking in relation to matters pertaining to bank resolution. However, at present the U.S. resolution regime does not fully align with the FSB requirements for cross-border cooperation.

With respect to the insurance sector, important gaps in the resolution framework remain that could undermine the regime’s ability to deal effectively with systemically important insurance

companies.¹ Due to the exclusion of insurance companies themselves from Title II of OLA, their resolution must be conducted under applicable state insurance laws that are not consistent with the KA. State resolution frameworks are directed primarily towards the protection of policy holders and provide for a largely court-driven, receivership process which may lead to delays - though it is recognized that the triggers for the commencement of insurance receivership are generally set at an early stage of the company's difficulties). Where an insurance company comes under a holding company, which can be resolved under OLA, an additional issue relates to the manner in which state resolution authorities would coordinate with each other and with the federal authorities. The National Association of Insurance Commissioners (NAIC) has played an important role in promoting harmonization of state insurance resolution laws; however, these frameworks do vary, to some degree and such variance could, along with the factors highlighted above, hinder the prompt resolution of a systemically important insurance group.

A summary of the consistency of the U.S. bank and insurance resolution regimes with the Key Attributes is set out below.

Scope, resolution authority and resolution powers (KA 1-3)

The scope of the resolution regime should be extended to cover all systemic firms and branches. The OLA covers financial institutions that are systemically significant or critical at the point of failure, including holding companies and nonbank financial companies, with the exception of insurance companies and systemic U.S. branches of foreign banks. To ensure alignment with the KA, the U.S. resolution regime, as enshrined in the DFA, should apply also to systemic insurance companies and to systemic U.S. branches of foreign banks; for branches, this extension should be tailored with a view to achieving a cooperative solution with foreign resolution authorities.

The resolution mandate of the FDIC is clearly defined in the legal framework. The FDIC's statutory objectives and functions are broadly in line with the KA and it is subject to a robust accountability and transparency framework. Adequate legal protection for actions taken, and omissions made, within the scope of its powers are in place. However, with respect to systemically important insurance companies, significant uncertainties arise with respect to the allocation of responsibilities between the FDIC—which, under certain circumstances provided in the DFA, is authorized to file the necessary judicial action to place an insurance company into receivership—and the relevant state insurance commissioners.

As noted above, the resolution regime under the DFA and for banks under the FDI Act is closely aligned with the KA. However, further clarity should be afforded to the statutory grounds for initiating resolution proceedings, in particular to make clear they apply suitably early at a point of non-viability. To ensure operational continuity of a covered financial company under resolution,

¹ Recognizing that the failure of a complex insurance group can, in principle, adversely impact financial stability and/or the functioning of the broader economy, the KA make relatively few adjustments for the specific features of insurance activities as compared to banks.

the FDIC should be provided with the explicit authority to require group entities to continue providing essential services to the entity in resolution, its successor (including a bridge entity under the SPE strategy) or an acquirer.²

The suite of resolution powers available under state law warrants expansion. The U.S. insurance regime is primarily designed for the purpose of protecting policy holders and provides state commissioners broad authority to rehabilitate or liquidate distressed insurance companies via procedures with state court approval, generally after notice and a hearing. Those tools more traditionally used for insurance companies, including run-off and powers to suspend and write-down policy holders, are available to state commissioners, but they do not comprise a complete set of the resolution powers envisaged under KA3 (e.g., bail-in, temporary stay) which should be addressed by extending the OLA powers to systemically important insurance companies.

At the same time, the challenges involved in applying the draft AM to insurance companies should be noted. It remains a subject of debate as to what degree the KA and the AM may need further modification to address the specific features of insurance companies.³ These are questions which may require further discussion within the international community.⁴

Supporting features and legal safeguards (KA 4-5)

Resolution safeguards envisaged in the DFA and FDI Act are generally consistent with the KA, but there is some scope for improvement, particularly with respect to state insurance resolution regimes. The exercise of resolution powers is subject to appropriate safeguards and due process requirements. The DFA and FDI Act provide for the necessary flexibility to take timely action, with court procedures not compromising the effective implementation of resolution measures. While legal remedies under the FDI Act—in contrast with DFA—are not explicitly limited to monetary compensation, there is no precedent for the FDIC being removed as receiver, or its actions otherwise being reversed. Moreover, the DFA and FDI Act provide for sufficient safeguards to prevent the exercise of early termination rights that arise solely by virtue of a failed firm's entry into resolution or the exercise of resolution powers against that firm. The FDI Act may, however, be enhanced by empowering the FDIC to override certain early termination rights for contracts of a resolved bank's subsidiaries and affiliates. With respect to insurance companies, state law does not typically provide for safeguards against the exercise of early termination rights in financial contracts. Moreover, the time that may be necessary for the exercise of resolution powers may not, in all cases, be fully consistent with the requirements of the timelines envisaged in the KAs.⁵ These weaknesses would be addressed however, by extending the application of OLA to insurance companies. Finally,

² By assuming control of the covered financial company the FDIC may be able to ensure continued provision from subsidiaries, but not necessarily other group entities.

³ Including by the FSB's Cross-border Crisis Management Group for Insurers.

⁴ These issues are discussed in greater detail in paragraphs 40-41 below.

⁵ See paragraphs 40-41.

the authorities are recommended to identify all disclosure requirements that may warrant explicit and temporary disclosure exemptions under OLA, and finalize any related regulatory documentation.

Funding in resolution (KA 6)

Financing arrangements under the DFA are consistent with the KA, but the state insurance arrangements are unequipped to support the resolution of systemically important insurers.

The Orderly Liquidation Fund (OLF) can borrow from the U.S. Treasury to fund a resolution, to be repaid from the proceeds of the sale of the failed company's assets or, to the extent that such proceeds are insufficient, through risk based assessments on the financial sector. Under state law, resolution funding is provided via a nationwide system of guarantee funds. The funds are legally required to protect policy holders in the event of insolvency, but they are not required to do so prior to insolvency. While the guarantee associations (GA) for life and health insurance could, in principle, help finance some resolution measures such as portfolio transfer prior to insolvency, there is no certainty that they would do so. Moreover, under current legislation, the funds are authorized to borrow from commercial banks or issue bonds, but not from the public sector. The liabilities of the failed insurance company are generally paid out over an extended period and are typically funded from the assets of the estate. However, it is unclear whether the financial capacity of the funds would be sufficient to address the failure of a systemically important insurer.

Cross border cooperation (KA 7-9)

At present, the U.S. resolution regime is not aligned with FSB requirements on cross-border cooperation. To enable effective cross-border coordination and achieve cooperative solutions with relevant foreign authorities, the KA prescribe that jurisdictions provide for transparent and expedited processes to give effect to foreign resolution measures, either by way of mutual recognition or by taking measures under the domestic regime that support resolution measures taken abroad. In the case of banks, a general statutory mechanism to give prompt legal effect in the United States to foreign resolution actions does not exist. Moreover, the depositor preference rules, which effectively subordinate claims from depositors at foreign branches of U.S. banks vis-à-vis claims from domestic depositors, is not in line with the KA, as it comprises discriminatory treatment on the basis of the location in which the claim is payable. Finally, the prospect of ring-fencing the assets of U.S. branches of foreign institutions, aimed at preserving such assets to the primary satisfaction of U.S. creditors, may undermine cross-border cooperation.

Crisis management groups (CMG) provide the U.S. authorities with important fora for enhancing the preparedness for, and facilitating the management and resolution of, cross-border distress. For the systemically important banks, in particular, the CMG have enabled a dialogue with host authorities about firms' recovery strategies; legal rights, duties and obligations under U.S. regime and host jurisdictions; and firm-specific resolution strategies and steps to improve resolvability. Moreover, recent discussions have focused on the nature, amount and distribution of gone-concern loss absorbing capital that may be required to recapitalize the relevant firms under OLA. For the systemically important insurers, the process is less advanced, reflecting the later

establishment of CMGs, but progressing along similar lines. The first phase of the finalization of cross-border coordination agreements that the authorities have been discussing with key hosts has been completed, involving 21 authorities from 11 jurisdictions for all seven U.S. G-SIBs with significant cross-border operations. This development is a positive step in facilitating cross-border resolution. Current arrangements for coordination with host authorities from jurisdictions that are not represented on CMGs, but where the local activities of U.S.-based firms could be systemically significant or critical at the point of failure, need to be aligned with FSB (draft) guidance.

Recovery and resolution planning (KA 10-11)

A comprehensive framework for the development of firm-developed resolution plans (also referred to as “living wills”) seeks to facilitate effective resolution. Pursuant to the DFA and FDIA, all bank holding companies with consolidated assets of at least \$50 billion; non-bank financial companies (NBFC) that are subject to supervision by the Federal Reserve Board (FRB) (including systemically important insurance holding companies) and IDI with total assets of \$50 billion are required to prepare, and update on an annual basis, plans for their rapid and orderly resolution under the U.S. Bankruptcy Code in the event of material financial distress or failure. In addition to supporting the FDIC’s planning for the exercise of its authorities under the OLA, the detailed plans enhance the agencies’ understanding of firms’ structures and potential impediments to resolvability.

Regulatory guidance, in combination with firm-specific feedback, is supporting iterative improvements of the living wills, but further efforts are needed in the insurance sector. Taken as a whole, the guidance for banks is extensive and provides for a robust underpinning of the living wills. However, specific standards for recovery and resolution plans of complex insurance groups, taking into account the specific characteristics of the insurance business (such as their funding sources, maturity profile of their liabilities and critical functions and critical shared services), remain underdeveloped—to some extent reflecting a lag in the development of international best practices in this area. The preparation of further insurance-specific guidance on the contents of the companies’ living wills, (e.g., on issues such as the identification of critical functions, the appropriate capital structure for an insurance group, and the development of appropriate resolution strategies) where appropriate aided by a horizontal review of the submissions from the U.S.-based globally systemically important insurer (G-SII), is imperative, also to provide the FDIC with relevant input for its own resolution planning activities under the OLA. In addition, the applicability of the SPE strategy on insurance groups warrants further analysis in view of the location of loss absorbing capacity and the close links between the liabilities and the corresponding assets.

While covered companies are making progress in the preparation of their plans, there are shortcomings that need to be addressed decisively. A communication from the FRB and FDIC, released in August 2014, identified a number of common weaknesses in the 2013 plans of the eleven largest banking groups, including (i) assumptions that the agencies deemed unrealistic or inadequately supported; and (ii) the failure to make, or even to identify, the changes in firm structures and practices that would be necessary to enhance the prospects for orderly resolution. The affected organizations have been instructed to improve their resolvability and update their Title

I resolution plans accordingly by July 2015. To ensure effectiveness of the planning process, and make sure that material impediments to resolvability are decisively addressed, efforts to closely scrutinize firms' plans need to be strictly pursued. In situations where identified shortcomings are not addressed in a timely manner, the authorities should stand ready to make use of their enforcement powers to cure deficiencies and make firms resolvable.

Access to information and information sharing (KA 12)

The arrangements allow the agencies access to information and the exchange thereof with domestic and international peers. The U.S. bank and insurance resolution regimes provide for adequate powers enabling the authorities to have access to information that is material for the planning, preparation and implementation of resolution measures, including via the recovery and resolution planning process.

INTRODUCTION

1. This review of the United States' resolution framework against the Financial Stability Board's KAs of Effective Resolution Regimes was completed as part of the FSAP update. It was conducted by Ross Leckow and Alessandro Gullo (Legal Department, IMF), Marc Dobler and Constant Verkoren (Monetary and Capital Markets Department, IMF), and Till Redenz and Masakazu Masujima (both external experts engaged by the IMF) from February 18 to March 9, 2015.⁶ The team reviewed the framework of laws, rules, guidance and arrangements in place as of the date of the completion of the review, as supplemented by information provided by the U.S. authorities as of May 2015, and held extensive meetings with U.S. officials, and additional meetings with banking and insurance sector experts and stakeholders (including auditors, lawyers, and associations). The team extends its thanks to the authorities who provided excellent cooperation.

2. The review covers the resolution frameworks that apply to the insurance and banking sectors only. The review of the banking sector is based upon a review of federal and state legislation and discussions with the three federal banking agencies (FBAs)—the FDIC, the FRB and the Office of the Comptroller of the Currency (OCC)—and a selection of state bank regulatory authorities. The review of the insurance sector is based upon a review of federal and state legislation (see paragraph 39) and discussions with the relevant federal agencies and bodies (including, the Federal Insurance Office (FIO) and the FRB) and state-level agencies and bodies (including, the NAIC, as well as selected state insurance authorities).

3. The U.S. authorities agreed to be evaluated according to the revised draft KA AM.⁷ Since the AM will not be finalized until it is tested in other countries, no ratings were assigned in this

⁶ The team gratefully acknowledges Ms. Dinah Knight, Senior Counsel, Legal Department for her advice and input on the US legal framework, and Ms. Laura Lorenzo, Research Officer, Legal Department, for her very helpful research assistance.

⁷ Dated 20 October 2014.

review. The authorities provided a comprehensive self-assessment as well as detailed responses to further questions. In keeping with the AM, the team did not have access to confidential recovery and resolution plans and accordingly, made no judgment as to the resolvability of individual firms. The parameters for the review are described in more detail below.

4. The evaluation was made in the context of the U.S. financial system’s structure and complexity. The AM must be capable of application to a wide range of financial sectors with varying degrees of complexity. To accommodate this breadth, a proportionate approach is adopted commensurate with the complexity, interconnectedness, size, risk profile and cross-border reach of the financial system under review. A review of compliance with the KAs is not, and is not intended to be, an exact science. Judgment is required and a review of one jurisdiction may not be directly comparable to another.

A. Institutional and Market Structure—Overview

5. The United States has a large, diverse financial sector with assets equivalent to 480 percent of gross domestic product (GDP). The system has global implications reflecting not only its sheer size—for example, the eight U.S. G-SIBs account for 22 percent of the total assets of all the G-SIBs—but also the high potential for spillovers and implications for cross-border operations and flows, highlighted during the global financial crisis. Depository institutions (mostly banks), pension funds, mutual funds and insurance companies account for around 70 percent of the financial sector assets.

Banking sector⁸

6. The banking sector holds 16 percent of all assets held by financial institutions and remains less concentrated than peer countries. Banks are the second largest financial sector after pension funds. The overall number of banks has been on a downward trend since early 1990s and reached an all time low in first quarter of 2014. While the U.S. banking system is less concentrated than in other industrialized countries, the five largest banks account for about 45 percent of the U.S. banking system’s total assets (twice the share of 10 years ago).

7. Banks’ balance sheets and income statements have strengthened. The total number of firms on the FDIC’s problem bank list has fallen to 329 at end September 2014, from a peak of 888 in March 2011.⁹ Compared to before the crisis, banks now hold more liquid assets, grant fewer loans and hold fewer trading account assets (both in absolute and relative terms). At the same time, banks have attracted more deposits, hold more capital, and are less leveraged. Profits have reached pre-crisis levels (in nominal terms) mainly due to lower provisions and lower interest expenses. However, the results from the Comprehensive Capital Analysis and Review stress tests show that, if

⁸ Unless otherwise stated, figures used in this section refer to December 2013.

⁹ These banks, have a supervisory rating of four or five on the supervisory scale, and combined assets of US\$126 billion.

hit by a severe global market shock, banks' capital ratios would fall significantly and banks would face sizable losses on their loan portfolios and trading activities.¹⁰

Insurance sector

8. The U.S. insurance market is the largest in the world. The insurance sector assets correspond to a half of banking sector assets and life insurers account for the largest portion. There were 4,538 insurance companies reporting to the NAIC at the end of 2013. The total premium volume in 2013 of \$1.56 trillion accounted for 33 percent of the global market. There are three main sectors—life, property and casualty (P&C), and health insurance. Key specialist insurance lines (i.e., those which must be written in separate companies) are financial guaranty, mortgage insurance, and title insurance. The insurance sector in the United States is less concentrated than in other industrialized countries. Most of the large insurance groups are domestically owned and although there are internationally active insurance groups, most business is written in relation to U.S. risks. There are no large conglomerate groups offering both banking and insurance services. Four large insurance groups¹¹ do however have deposit-taking institutions and are regulated by the FRB as Saving & Loan Holding Companies (SLHCs). Three U.S. insurers, American International Group (AIG), MetLife, and Prudential have been identified as G-SIIs by the Financial Stability Board (FSB).

9. The insurance sector has been gradually improving its capital position in recent years but risks remain. Capital adequacy at the legal entity level, measured by the regulators' risk-based capital (RBC) requirements, has improved since the financial crisis. Large life insurance groups have expanded non-traditional insurance products. Although the investment risks fall to policyholders, insurers typically provide (often complex) guarantees to policyholders and are exposed to significant risk if economic growth falters again or remains low for long. Direct writers of life insurance, annuities and health products like disability income and long-term care will face the greatest risk due to the long-term nature of their interest guarantees.

Securities and derivatives markets

10. The debt securities market is dominated by corporate debt securities, treasury securities and Government-Sponsored Enterprises (GSE) backed securities. The nominal value of outstanding debt securities at end-2013 amounted to about \$39 trillion (230 percent of GDP). Corporate bonds, including Asset Backed Securities (ABS), accounted for a third of this, of which half were issued by non-financial corporations and 10 percent by ABS issuers (down from 30 percent before the crisis). GSEs are the only segment that is now larger than before the crisis.

11. The U.S. derivatives market represents one third of the world market. The notional amount of outstanding derivatives contracts, which totaled \$237 trillion at end 2013, has been

¹⁰ <http://www.federalreserve.gov/newsevents/press/bcreg/20150305a.htm>

¹¹ TIAA-CREF, State Farm Mutual, Nationwide Mutual and USAA.

relatively stable since 2010.¹² The market is dominated by a small group of large financial institutions—four large commercial banks represent 93 percent of the total banking industry notional amounts. Derivative contracts are concentrated in interest rate products, which comprise 82 percent of total derivative notional amounts. Swap contracts represent the bulk of the derivatives market (64 percent of all notional amounts) followed by futures and forwards (18 percent) and options (14 percent).

B. Review of the Preconditions for Effective Resolution Regimes

Precondition A: A well-established framework for financial stability, surveillance and policy formulation¹³

12. Title I of the Dodd Frank Act (DFA)¹⁴ established the Financial Stability Oversight Council (FSOC) charged with monitoring and identifying emerging risks to financial stability across the entire financial system, identifying potential regulatory gaps, and coordinating the agencies' responses to potential systemic risks. The FSOC is composed of the Treasury Secretary (who is also the chair); the heads of the three FBAs; the heads of the Consumer Financial Protection Bureau (CFPB), Securities and Exchange Commission (SEC), Commodity Futures Trading Commission (CFTC), Federal Housing Finance Agency (FHA), and National Credit Union Administration (NCUA); and an independent member with insurance expertise appointed by the President and confirmed by the Senate. Members are advised by the Directors of the OFR and the FIO—new U.S. Treasury offices created by DFA—and by nominated representatives of state insurance commissioners, banking supervisors, and securities commissioners. One of the FSOC's tasks is the designation, as appropriate, of nonbank financial companies if the FSOC determines that material financial distress at the nonbank financial company, or the nature, scope, size, scale, concentration, interconnectedness, or mix of the activities of the nonbank financial company, could pose a threat to U.S. financial stability. Once designated, these nonbank financial companies are subject to consolidated supervision by the FRB and to enhanced prudential standards. The FSOC has designated four nonbank financial companies—AIG, General Electric Capital Corporation, MetLife, and Prudential Financial—to date.

13. The DFA requires the FRB to conduct and publish summary results of annual stress tests of systemic nonbank financial companies and BHCs with \$50 billion or more in assets. Such companies also are required to conduct their own stress tests on a semiannual basis. The DFA requires financial companies with more than \$10 billion in assets to conduct annual stress tests in accordance with regulations established by the respective primary FBA.

¹² Based on derivatives activities of 1,383 insured US commercial banks and savings associations.

¹³ See separate Technical Note on Systemic Risk Oversight, Macroprudential Framework, for more detail.

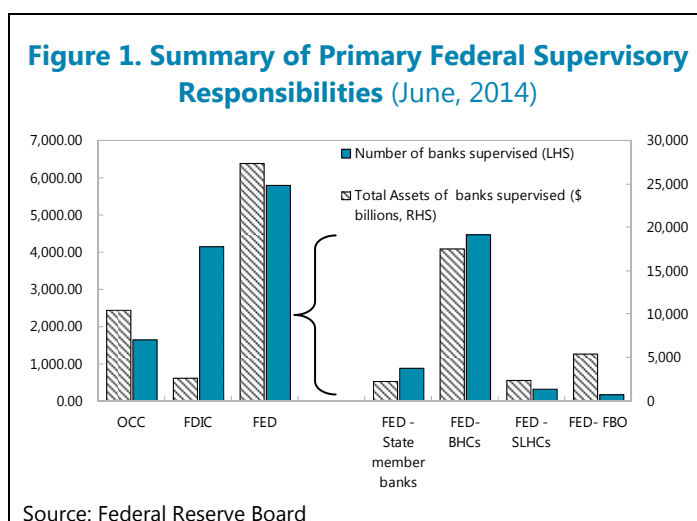
¹⁴ Formally the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.

Precondition B: An effective system of supervision, regulation and oversight of financial institutions

Banking supervision and regulation

14. The United States operates under a “dual banking system.” A bank charter may be issued by the federal government or by a state. Federal bank charters for national banks and federal savings associations are issued by the OCC. Each of the 50 states has a banking authority that charters banks under its own laws and regulations. These banks are generally referred to as “state banks” or “state savings associations.” Each U.S. bank, whether chartered under state or federal law, is subject to regulation, supervision, and examination by a primary FBA as follows:¹⁵

- **OCC:** Charters, regulates, and supervises all national banks and federal savings associations and licenses and supervises federal branches and agencies of foreign banks.
- **FRB:** Regulates and supervises state chartered banks that are members of the Federal Reserve System (“state member banks”). It is also responsible for regulating and supervising any company that owns or controls a national or state bank. Certain BHCs that, along with their depository institution subsidiaries, meet enhanced capital and managerial standards, may elect to become financial holding companies (FHCs) and engage in a broader array of financial activities, including securities, insurance, and merchant banking. The FRB is the consolidated supervisor of all BHCs, FHCs and SLHCs, which, like BHCs, may choose to be treated as FHCs if they engage in a broader array of financial activities, and their depository institution subsidiaries meet enhanced capital and managerial standards.
- **FDIC:** Regulates and supervises state banks that are not members of the Federal Reserve System (“nonmember banks”) and state chartered savings associations jointly with state banking authorities. In addition, as a consequence of its deposit insurance function, the FDIC has the authority to examine for deposit insurance purposes any bank, either directly or in cooperation with state or other federal supervisory authorities, and has “backup enforcement authority” over all banks. This means it can recommend that another federal



¹⁵ The DFA dissolved the Office of Thrift Supervision and transferred its regulatory and supervisory authority, with respect to SLHCs and savings associations to the FBAs: the FRB regulates SLHCs, the OCC regulates federally chartered savings associations, and the FDIC regulates state-chartered savings associations.

banking agency take action against a bank in appropriate circumstances and may take such action directly if the other agency does not take action.¹⁶

15. Foreign banking organizations (FBOs) have been able to conduct business in the United States broadly under the same powers, and subject to the same limitations, which apply to domestic banks. No FBO may establish a branch or an agency without the prior approval of the FRB. All banks and branches or agencies of FBOs have a primary federal regulator. If the FBO chooses a federal license for a branch or agency, then it is supervised and examined by the OCC. If an FBO elects to open a branch or agency under a state license, then it is typically examined by the state banking authorities and also by the FRB on a joint or alternate (i.e., rotating) basis.

16. Since the 2010 U.S. FSAP, important changes have taken place in the legal and regulatory framework for banks. The DFA requires that large BHCs and systemically designated nonbank SIFIs be subject to enhanced prudential standards; provides for the consolidated supervision of all designated nonbank SIFIs; gives the authorities enhanced resolution powers for nonbank SIFIs (see below); and provides for the strengthened supervision of systemically important payment, settlement, and clearing utilities. With regard to enhanced group powers, the DFA (i) tightens the limitations on transactions between a BHC, a subsidiary bank, and its affiliates; (ii) incorporates financial stability into the analysis of transactions governed by the Bank Holding Company Act (BHC Act) and the Bank Merger Act;¹⁷ (iii) incorporates financial stability considerations into the supervision of holding companies and enhances the requirement for holding companies to be eligible to engage in expanded activities; (iv) generally eliminates the limitations under the Gramm-Leach-Bliley Act that restricted the FRB's ability to examine, obtain reports from, or take enforcement action against a functionally regulated subsidiary of a BHC, such as a broker-dealer or insurance company;¹⁸ (v) authorizes the FRB to examine the activities of nonbank subsidiaries of holding companies—other than functionally regulated subsidiaries—subject to the same standards, and with the same frequency as if such activities were conducted in the organization's lead subsidiary depository institution; (vi) prohibits a depository institution that is subject to a formal enforcement order with respect to a significant supervisory matter from converting its charter except under certain circumstances.

17. Regulations also require that FBOs with U.S. non-branch assets of \$50 billion or more establish a U.S. intermediate holding company (IHC). The foreign-owned U.S. IHC generally will be subject to the same risk-based and leverage capital standards applicable to U.S. bank holding

¹⁶ The FDIC also has statutory authority to examine the affiliates of any insured depository institution.

¹⁷ DFA Sections 163 and 604 require the appropriate federal banking agency to take into account risks to the stability of the US banking or financial system in approving the relevant applications under the BHC Act and the Bank Merger Act. Similarly, section 173 adds financial stability to the list of factors that the Federal Reserve may consider when acting on an application by a FBO to open an office in the US. Specifically, the Federal Reserve may consider whether, for a foreign bank that presents a risk to the stability of the US financial system, the FBO's home country has adopted or is making demonstrable progress toward adopting a financial regulatory system that mitigates such risk.

¹⁸ The Federal Reserve must continue to rely on examinations conducted by the subsidiary's primary bank supervisors or functional regulators to the fullest extent possible.

companies. It will include (with some exceptions) all its U.S. bank and nonbank subsidiaries (e.g., broker-dealers, finance companies, and special purposes entities) but not foreign branches. IHCs will be subject to the Federal Reserve's rules requiring regular capital plans and stress tests.

18. The assessment of the Basel Core Principles for Effective Supervision (BCP)¹⁹ found that the FBAs have improved considerably in effectiveness since the previous FSAP but the system remains fragmented. In response to global and domestic reforms, particularly the DFA, the FBAs have stepped up their supervisory intensity, especially for large banking organizations, putting emphasis on banks' capital planning, stress testing and corporate governance. To match, the FBAs have also enhanced their supervisory capacity, adding significantly to their staffing numbers and skills base. These improvements were reflected in the high degree of compliance with the BCP assigned under the assessment. Shortcomings were observed particularly in the treatment of concentration risk and large exposures, but they did not raise concerns overall about the authorities' ability to undertake effective supervision. It was also noted that many requirements of the BCP are not established in U.S. law, regulation, or supervisory guidance, rather are in practice determined by the supervisor. While the legislative reforms delivered some rationalization of supervisory responsibilities they did not fundamentally address the fragmented regulatory system. The problems inherent in multiple regulators with distinct but overlapping mandates remain, with the new challenge of delineating responsibilities with a stand-alone consumer protection agency. While the FBAs are committed to making the revised arrangements work and cooperation has clearly improved, substantial duplication of effort remains.

Insurance supervision and regulation

19. Since the last FSAP, important changes have also taken place in the supervisory framework for insurance firms. In contrast to the banking sector, the insurance sector is primarily regulated and supervised at the state level. The establishment of the FIO has created a mechanism for identifying national priorities for reform and development. The extension of the FRB's responsibilities to cover consolidated supervision of insurance groups has strengthened supervision of the affected groups (which now cover around 30 percent of total premium income in the United States.). State regulators have also been progressing important reforms such as the solvency modernization initiative, strengthening group supervision and international cooperation. The role of each authority is as follows:

- **State regulators:** State insurance departments carry out licensing, supervision and examination of insurance companies and intermediaries under powers set out in state legislation. A commissioner heads the department and exercises all formal powers. Some commissioners are elected, but most are appointed by the state governor. While arrangements vary among states, funding is usually raised from the insurance markets via fees and levies. Insurance departments' budgets are generally subject to the state budgeting

¹⁹ <https://www.imf.org/external/pubs/cat/longres.aspx?sk=42825.0>.

processes. Insurance departments also collect premium taxes for the states, which are a significant part of state governments' revenues.

- **NAIC:** The NAIC is a regulatory support organization for state insurers and plays an important role in promoting consistency across state regulation. Through NAIC, state regulators establish model laws, regulations, best practices, and examination handbooks, and coordinate their regulatory oversight. NAIC has around 470 staff, which compares with 11,529 employed by the states. NAIC's Financial Analysis Working Group is composed of 18 senior financial experts who review all "nationally significant companies" (around 1,600 companies, representing 85 percent of the market) based on annual and quarterly statements and other information. Their objective is to provide a peer review process for domestic state regulators, who retain responsibility for any action. NAIC has implemented a number of key reforms, some of which reflect the recommendations of the 2010 FSAP, including establishing supervisory colleges for all U.S. based internationally active insurance groups and an increasing number of memoranda of understanding between United States and international regulators.
- **FRB:** As part of the response to the 2008 financial crisis, the FRB was given responsibility to regulate and supervise large nonbank financial groups (including insurance groups). The FRB is not responsible for licensing or regulating individual insurance companies, but has a role in insurance regulation and supervision through its primary federal responsibility for consolidated regulation of: (i) BHCs—to the extent that there are one or more insurance companies as well as at least one bank in the group (there are no such groups at present); (ii) SLHCs to the extent that there are one or more insurance companies as well as at least one savings and loan company in the group—there are 15 such groups at present, including four of the largest insurers in the country; and (iii) FSO designated NBFCs that are, or have material subsidiary, insurance companies.
- **FIO:** The FIO was established in the Department of Treasury and has a broad monitoring role of the insurance sector and its regulation, a lead role in international aspects of insurance regulation and specific responsibilities in relation to systemic risk in the insurance sector. The FIO represents the United States in the International Association of Insurance Supervisors. The FIO has no authority to license or regulate insurance companies. In December 2013, it released a "Modernization Report" pursuant to Title V of the DFA, with 18 near-term recommendations for state regulators, and nine recommendations with regard to direct federal involvement, as well as proposals for reform to increase federal oversight of the sector over the long term.

20. Overall, the assessment of the Insurance Core Principles²⁰ found a reasonable level of observance of the standards. Regulation benefits from a sophisticated approach to legal entity

²⁰ <https://www.imf.org/external/pubs/cat/longres.aspx?sk=42826.0>.

capital adequacy (the risk based capital or RBC approach). Regulation and supervision continue to be conducted with a high degree of transparency and accountability. FRB supervision is bringing an enhanced supervisory focus to group-wide governance and risk management and peer group review and challenge through the processes of the NAIC is a source of strength. Lead state regulation is developing and a network of international supervisory colleges has been put in place. Cooperation between state and federal regulators is developing, but has further to go. Key areas to address include:

- The valuation standard of the state regulators, especially for life insurance, and group capital standards;
- Gaps in governance and risk management requirements and in market conduct and intermediary supervision;
- Governance and funding arrangements for state insurance regulators;
- The objectives of state regulators and scope for conflict between FRB objectives and policyholder protection;
- The complex and fragmented regulatory system.

21. The fragmentation at the supervisory level is replicated in the resolution context. Each of the 50 states has a distinct legal framework for insurance resolution and a distinct resolution authority (i.e., the state insurance commissioner). NAIC has played an important role in promoting greater uniformity in the legal and policy frameworks for resolution at the state level. In particular, it has, over the years, developed and promoted the adoption of model insurance resolution laws by its member states. Most states have based their legislative frameworks on one of these models.²¹ While each model law has sought to codify existing practice and precedent, the lack of complete harmonization could, to some extent, hinder the resolution of a systemically important insurance group that has multi-state operations.

Precondition C: Effective protection schemes for depositors, insurance policy holders and other protected clients or customers, and clear rules on the treatment of client assets

Banking sector

22. The United States has two federally-mandated deposit insurance schemes.²² Deposits in banks and savings associations (thrifts) are insured by the FDIC; while deposits in credit unions are

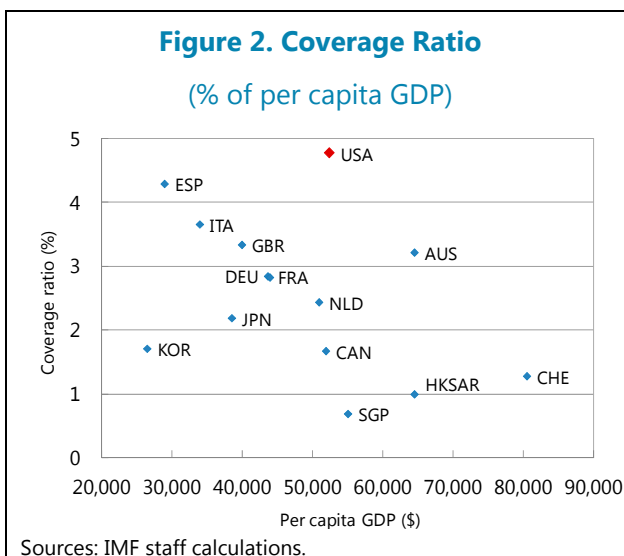
²¹ For example, in the supervisory context approximately 35 states have adopted NAIC's Insurance Holding Company System Regulatory Act. In contrast, approximately six states have adopted the 2007 Insurer Receivership Model Act while 28 have adopted the 1977 Model Act. Many other states rely on earlier model legislation promulgated by NAIC or its predecessor.

²² There is also a Depositors Insurance Fund (established in 1934) which offers unlimited insurance on deposits at Massachusetts chartered savings banks.

insured under a separate legislative mandate by the NCUA. Both cover deposits for each account ownership category, per depositor and institution up to the statutory limit of \$250,000. The FDIC manages the Deposit Insurance Fund (DIF) and the NCUA a National Credit Union Share Insurance Fund (NCUSIF); both are backed by the “full faith and credit” of the U.S. Government.

23. Deposit insurance coverage is high by international standards (Figure 2). The DFA

permanently raised the deposit insurance coverage to \$250,000, equivalent to nearly five times per capita GDP. Also, different account balances are not aggregated when determining coverage. Depositors can secure much higher total coverage by opening multiple accounts at the same bank under different “ownership capacities” e.g., an individual account, a joint account with a spouse, a trust account, and a retirement account each of which can be covered up to \$250,000. U.S. depositors are well aware of this treatment and structure their accounts accordingly.²³



24. Deposit insurance funds were depleted during the crisis. As noted in the 2010 FSAP, public confidence in the deposit insurance schemes remained high throughout the crisis, however, the paid-in deposit insurance funds proved inadequate. The DIF, which stood at \$52.4 billion or 1.22 percent of insured deposits prior to the crisis, reached a deficit of \$8.2 billion by end September 2009. As in the previous banking crisis the FDIC was forced to substantially increase assessments on the industry in a pro-cyclical way i.e., raising levies at a time of financial stress. Additionally, the FDIC’s line of credit from the U.S. Treasury was increased from \$30 billion to \$100 billion.

25. A number of measures were enacted following the crisis to strengthen the DIF but not the credit union scheme. The DFA raised the target minimum designated reserve ratio (DRR) to 1.35 percent (to be reached by end September 2020), from 1.15 percent (by 2016). However, the most important change was to remove the “hard cap” and give the FDIC Board discretion to set a higher target without having to cease assessments (and pay dividends) at 1.35 percent. Removing this cap was a recommendation of the 2010 FSAP and the FDIC Board has used the discretion to set a two percent target. The credit union scheme is unchanged, however, and requires reform.

²³ The FDIC offers an example of how a family of five could structure their accounts to secure US\$3.5 million of coverage at the same bank https://www.fdic.gov/deposit/deposits/brochures/your_insured_deposits-english.html.

Insurance sector

26. Insurance policyholders are protected against loss arising from the insolvency of insurance companies by state guaranty associations. All U.S. insurance companies are required to be members of associations covering life and health insurance and, through separate organizations, property and casualty. These associations are established by state laws (based upon NAIC's Life and Health Insurance Guaranty Association Model Act and Property and Casualty Insurance Guaranty Association Model Acts). Payments are triggered by the insolvency of an insurer and the issuance of an order of liquidation. Laws differ on the extent of coverage and maximum amount per policyholder (between \$100,000 and \$500,000 depending on the product and state). Liabilities that require coverage are typically paid out over a number of years. Associations rely primarily on estate assets to fund their payment obligations. The Guaranty System has access to additional funds through ex post assessments of other insurers writing the same class of business in the same state to make payments to policyholders, i.e., it is not pre-funded. State laws set limits on assessment—typically, at 2 percent per year of each insurer's prior year premium income in the state.

Precondition D: A robust accounting, auditing and disclosure regime²⁴

27. U.S. accounting standards (U.S. GAAP) are established by the Financial Accounting Standards Board (FASB). Both the FASB and International Accounting Standards Board are currently working on a convergence program, designed to bring U.S. and international financial reporting standards into a single framework.

28. Financial statement audit requirements are robust, having been considerably strengthened in 2002 with the passage of the Public Company Accounting Reform and Investor Protection Act (also known as the Sarbanes-Oxley Act). The Sarbanes-Oxley Act enhanced audit scrutiny, toughened auditor independence requirements, required various management attestations about the reliability of financial accounts, and expanded disclosure requirements with the objective of providing the users of financial statements with greater security as to their accuracy and reliability.

Precondition E: A well-developed legal framework and judicial system

29. The United States possesses an independent judiciary and well-regulated accounting, auditing, and legal professions. The judicial system is comprised of both federal and state systems. Judges in both federal and state courts must be members of the bar and generally have significant experience as practicing lawyers before becoming judges. Federal judges are appointed by the President with the advice and consent of the Senate and receive lifetime appointments. States vary in their methods of judicial appointment. Some follow a system similar to the federal system, i.e., the

²⁴ This is a summary of existing FSAP documents. For detailed information on market discipline, accounting and auditing framework, see separate IOSCO assessment.

state governor appoints judges with some input from the legislature. Some states, however, appoint judges through a general election.

30. Lawyers must receive a license to practice law from a state or states. All states but one (Wisconsin) require applicants who are not already members of another state's bar to pass a bar examination prior to receiving a license. In addition to controlling admission into the profession, the states also regulate the profession. Regulation is often delegated to a self regulatory organization, i.e., a state bar association. Lawyers are also subject to ethical standards set by the states.

C. Resolution Regime Reforms

31. The resolution regime for financial institutions has been significantly enhanced since the financial crisis. Title II of the DFA creates an OLA that permits the FDIC to be appointed as receiver for a failing systemically important financial company (formally a "covered financial company")²⁵ whose disorderly collapse would pose substantial risks to the financial system and the broader economy. The definition of "financial company" and thereby scope of application of Title II are (i) bank holding companies; (ii) nonbank financial companies that are supervised by the FRB pursuant to section 113 of the DFA; and (iii) financial companies that are predominantly engaged in activities that are financial in nature or incidental thereto as set forth in FRB regulations.²⁶ In addition, subsidiaries of companies described above, other than a subsidiary that is an IDI or an insurance company, may be resolved using OLA powers if they are predominantly engaged in activities that are financial in nature or incidental thereto. Title II is triggered only by a recommendation of two-thirds of the directors of both the FRB and the board of the FDIC and a determination by the Secretary of the Treasury, in consultation with the President (sometimes referred to as the "three keys process"), that *inter alia* the company is in default or in danger of default; the failure of the company and its resolution under otherwise applicable federal or state law would have serious adverse effects on financial stability in the United States; resolution under the bankruptcy law would not be appropriate; and resolution under the new regime would avoid or mitigate these adverse effects. The SEC or the FIO would substitute for the FDIC in the "three keys" recommendation process if the firm or its largest domestic subsidiary is, respectively, a broker-dealer or an insurance company, with the FDIC being consulted in both cases.

32. Title II of the DFA gives the FDIC, as receiver for the failed SIFI, powers similar to those it has when acting as a receiver for a bank. Specifically, the FDIC may stabilize the company with loans or guarantees, sell assets or operations, and transfer assets and liabilities to a bridge company.

²⁵ A "financial company" that becomes subject to the OLA is defined as a "covered financial company." If it is a broker-dealer registered with the SEC and a member of the Securities Investor Protection Corporation (SIPC) the FDIC must appoint the SIPC to act as trustee, with the powers and duties provided by the Securities and Investor Protection Act (SIPA), for those assets and liabilities not transferred to a bridge financial company by the FDIC.

²⁶ The final rule issued by the FRB on April 3, 2013 and codified in code of Federal regulations (CFR) 242.3 makes clear that the activities of mutual funds, private equity funds, hedge funds and other pooled investment vehicles are "financial activities" and defines a company "predominantly engaged in financial activities" as one with 85 percent or more of its assets or revenues derived from such activities.

The act requires the FDIC to ensure that creditors and shareholders of the failed company bear losses and that directors and management responsible for the company's failure are removed.

33. The DFA also allows the FDIC to obtain temporary funding for a resolution by borrowing from the Treasury via the OLF subject to certain limits.²⁷ Importantly, any borrowings from the Treasury must be repaid through proceeds from the sale of the failed company's operations. If such proceeds are insufficient to fully repay all borrowings from the Treasury, assessments would be made on certain creditors of the failed firm and, if necessary, on financial companies, including bank holding companies that have \$50 billion or more in total assets, and nonbank financial companies supervised by the FRB. One final provision of importance is the prohibition on taxpayers bearing any losses in the resolution of a company that has been put into receivership under Title II.²⁸ This provision seeks to prevent any future government bailouts for failing financial institutions, no matter how systemic their failure might be.

34. The following types of financial institutions cannot be resolved using the OLA powers:

- **IDIs:** IDIs (i.e., banks and savings and loans associations)²⁹ including those that could be systemically significant or critical in the event of failure, are excluded from the definition of financial company and resolved pursuant to the FDI Act.
- **U.S. branches of FBOs:** Uninsured³⁰ branches of FBOs operating in the United States must have either a state or federal license. With respect to a federally licensed branch of a FBO, the legal framework in the United States generally provides that such a branch is resolved in accordance with Federal law—specifically, the International Banking Act (IBA). The two largest federally licensed branches had assets of about \$80 billion at end of September 2014. One of these, however, has grandfathered deposit insurance and would be resolved under the FDI Act (see essential criteria 1.2). The legal framework generally provides that a branch of a FBO that is licensed by a state is resolved by the state resolution authority in accordance with that state's law. The ten largest state-licensed branches by assets (ranging from \$78 billion to \$150 billion at end September) are New York licensed. There may be cases, however, where the resolution framework under Federal law would apply to the property and assets of a state-licensed branch.³¹

²⁷ See EC 6.1 for further details.

²⁸ See DFA Section 214.

²⁹ Credit Unions are resolved pursuant to the Federal Credit Union Act (FCUA) and their resolution is not covered under this assessment.

³⁰ FBOs have not been able to establish insured branches in the US Since December 19, 1991, however, insured branches operating at that time were permitted to continue operating with deposit insurance, of which currently ten remain. These insured branches would be resolved by the FDIC under the FDI Act. See 12 USC. § 1821(c).

³¹ Specifically where a FBO has one or more State-licensed branches or agencies and one or more federally licensed branches or agencies, and the OCC appoints a receiver for the Federal branch or agency, the receiver shall take

(continued)

- **Insurance companies:** Insurance companies (as opposed to their holding companies) cannot be resolved using the OLA powers, and are also not subject to the Federal Bankruptcy Code, instead they must be resolved pursuant to state legislation. A resolution proceeding for an insurer is referred to as a “receivership,” and may take the form of conservation, rehabilitation or liquidation. A receivership can be commenced against an insurer in the insurer’s domiciliary state (the state in which the insurer is incorporated), and is governed by the law of that state. In some circumstances, the laws of other states may also be implicated. For example, a guaranty fund in a state in which a policyholder of the insolvent insurer resides is governed by that state’s law. As a result multiple state legislation and state guaranty funds would come into play in the failure of a large insurance group writing business across multiple states. Title II provides that if the appropriate state regulator does not commence the resolution of the insurance company within 60 days of a systemic risk determination by the Treasury Secretary with respect to the insurance company, then the FDIC shall have the authority to stand in the place of the appropriate regulatory agency and file the appropriate judicial action in the appropriate state court to place such company into orderly liquidation under the laws and requirements of the state.

35. A comprehensive recovery or resolution planning process helps to promote resolvability of complex financial firms. The U.S. authorities view recovery planning as an integral part of the framework for the consolidated supervision of large financial firms. Hence, such firms are expected to prepare, and periodically update, plans for remedying potential financial or operational weaknesses via predefined recovery options. In addition, Title I of the DFA³² mandates certain firms (i.e. all BHCs with consolidated assets of at least \$50 billion and each NBFC that is supervised by the FRB) to produce plans for their rapid and orderly resolution under the U.S. Bankruptcy Code in the event of material financial distress or failure.³³ These so-called “living wills” provide the FDIC, in its capacity as receiver under OLA, with a thorough understanding of, among others, the firms’ structures, critical functions and critical shared services, and intra-group financial linkages and funding sources. In turn, the living wills can inform resolvability assessments prepared by the FDIC for financial firms whose failure could adversely impact U.S. financial stability. Moreover, they support the FDIC’s own planning for the exercise of its OLA under Title II of the DFA (and the FDI Act, as appropriate). In principle, the power to require firms to take measures that seek to remove obstacles to resolvability under Title I, as provided to the FRB and FDIC, can also contribute to achieving greater resolvability under OLA.

36. The FDIC has focused on developing a SPE strategy for deploying OLA powers.³⁴ SPE is a resolution strategy that would take advantage of most U.S. SIFIs being organized under a non-

possession of all the property and assets of such FBO in the United States, not only the property and assets of the Federal branch. See 12 USC. § 3102(j).

³² Section 165(d) of Title I sets out living will requirements, while Title II establishes the OLA powers.

³³ Similar requirements exist under the FDI Act for IDIs with total assets of at least US\$50 billion.

³⁴ See https://www.fdic.gov/news/boarrpah d/2013/2013-12-10_notice_dis-b_fr.pdf.

operating parent holding company structure, either a BHC or a FHC, which are required to act as a “source of strength” to their banking subsidiaries.³⁵ Their balance sheets predominantly comprise long-term debt and investments and loans in subsidiaries, with the operating liabilities of the group³⁶ typically residing at the operating company (e.g., bank) level. The FDIC would initiate an OLA receivership at a single point, the top tier U.S. holding company, while the group’s operating subsidiaries (e.g., IDI, broker-dealer etc.) would not be subject to a resolution proceeding. This would have the significant benefit of keeping numerous group subsidiaries and affiliates interconnected through legal structure, funding sources, intra-company arrangements (including cross-default provisions and cross-guarantees) and group services, open for business. The FDIC would immediately establish a bridge financial company into which it would transfer the assets of the parent holding company, including ownership interests in, and intercompany loans to, these operating subsidiaries. Rights related to equity, subordinated debt and senior unsecured debt of the holding company would be terminated, leaving only a residual claim on the receivership. Under the SPE strategy these residual claims would be met through a securities-for-claims exchange six to nine months later, in a new (and listed) financial company, which would assume the assets and liabilities of the bridge bank. The effect would be to bail-in the creditors of the failed holding company and recapitalize the group, via the parent bridge providing capital and liquidity as needed to subsidiaries (see EC3.10 for further details).

37. Making an SPE workable in practice requires a number of challenges to be resolved.

Adequate capital and debt needs to be issued by the holding company so that sufficient quantities can be bailed-in to cover the group’s losses, support subsidiaries and restore market confidence in the bridge and successor entity. The FSB recently issued a proposal³⁷ for minimum total loss absorbing capital (TLAC), including internal TLAC for G-SIBs.³⁸ Other challenges include giving cross-border effect to resolution measures; preserving critical access to Financial Market Utilities; and ensuring the continuity of essential group operational services (e.g., group treasury, human resources and IT services). With regard to the former, the recent International Swaps and Derivatives Association (ISDA) Resolution Stay Protocol (see EC4.3) adopted by 18 global major banks is a positive development but further reforms are required. Many of the remaining impediments are intended to be addressed through effective recovery and resolution planning. Progress on these issues is essential for a successful implementation of a SPE strategy under Title II.

³⁵ The BHC Act (§ 225.28) defines source of financial strength to mean, “the ability of a company that directly or indirectly owns or controls an insured depository institution to provide financial assistance to such insured depository institution in the event of the financial distress of the insured depository institution.”

³⁶ Short-term liabilities arising from the primary business of the financial group e.g., deposits and repos.

³⁷ <http://www.financialstabilityboard.org/wp-content/uploads/TLAC-Condoc-6-Nov-2014-FINAL.pdf>.

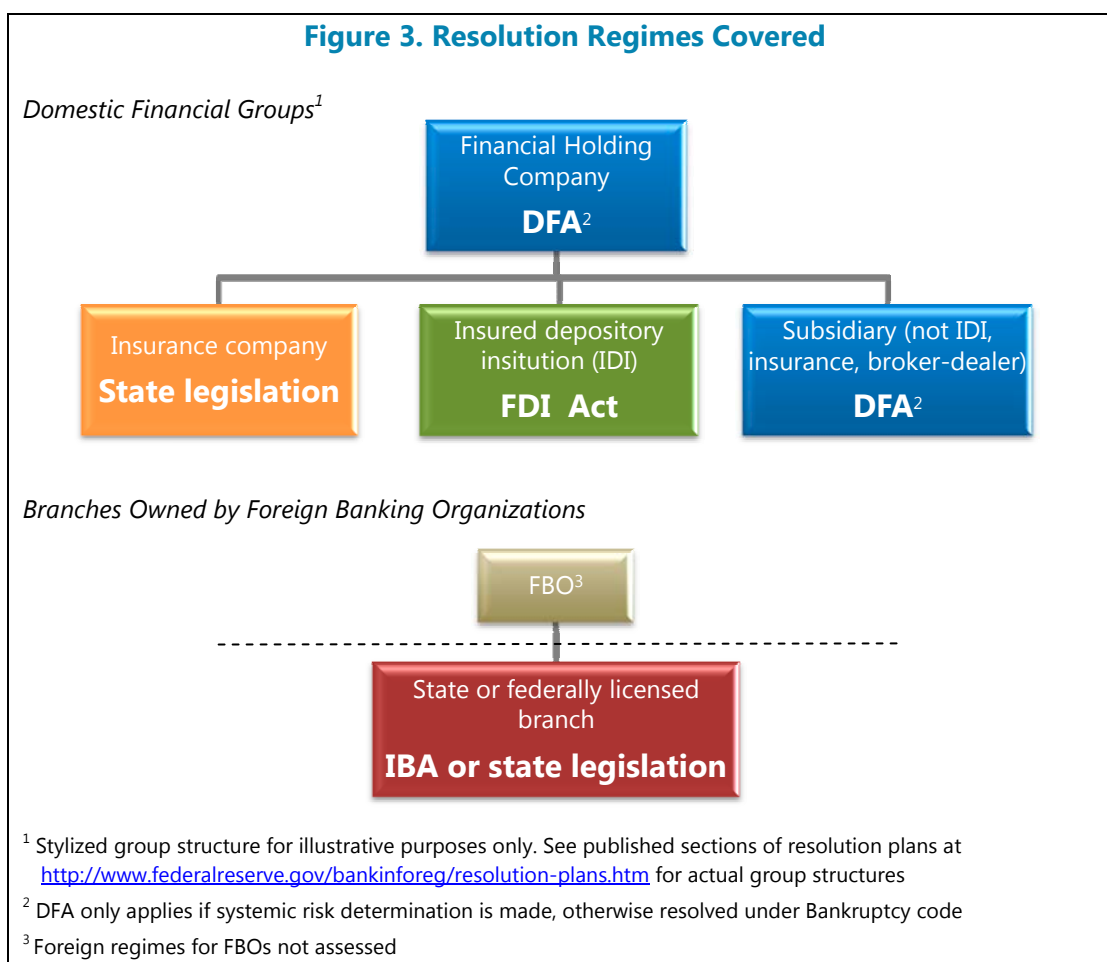
³⁸ Internal TLAC would take the form of debt or equity claims of a parent on its subsidiary, and that would enable losses in a troubled subsidiary to be up-streamed the parent via the conversion or write-down of the intra-group claim. This up-streaming could happen outside resolution if the subsidiary meets certain contractual or statutory criteria (e.g., capital hurdle rates, point of non-viability) or in resolution. There is also a cross border element in that credible TLAC could provide assurance to host authorities of cross-border subsidiaries that support will be provided by the parent, reducing the incentives for ring fencing.

38. The challenges may be more substantive for insurance groups. Insurance companies have different liability structures than banks that may lend themselves more to a MPE resolution strategy, where different entities in the group including at the operating level enter separate resolution proceedings. Most loss absorbing capacity is at the level of the operational insurance subsidiaries, with a view to protecting policy holders at the state level. Moreover, much less progress has been made with regard to recovery and resolution planning for insurance groups and a significant added complication is the extensive communication and coordination that would be required between the FDIC, multiple state insurance regulators and potentially the insurance guaranty system to successfully implement a SPE strategy for an insurance SIFI.

DETAILED REVIEW

39. The table that follows sets forth a detailed review of the consistency of the U.S. resolution regime for the banking and insurance sectors with the KA. There are several parameters for this review that are worth noting at the outset:

- **First, the review is based upon a draft rather than a final version of the assessment methodology.**
- **Second, the review pertains only the banking and insurance sectors.** Accordingly, certain essential criteria (EC) are not reviewed in this exercise e.g., because they pertain to the resolution of financial market infrastructures.
- **In addition, within the banking and insurance sectors, there are multiple resolution regimes that are relevant.** As a result, the description and findings sections for most EC in the following table describe separately the resolution regime applicable to (i) “covered financial companies” under Title II of the DFA (which generally may include systemically important holding companies for banks and insurance companies, as well as nonbank/noninsurance company subsidiaries of those holding companies); (ii) domestic banks under the FDI Act, and U.S. branches of FBOs under the IBA and New York (NY) state law (the key jurisdiction for systemic branches) for KA 1 and 7; and (iii) the state resolution regime for insurance companies. Appendix I summarizes the resolution regimes which apply to different types of financial groups and companies in the United States. Figure 1 highlights the resolution regimes reviewed under this assessment. As it could not be assumed that all systemic banking and insurance companies could be resolved at the holding company level using Title II resolution powers (an MPE strategy may be preferred or prove necessary) the resolution regimes which apply at the operating company level also were reviewed.



- **Finally, it is not possible to provide a complete or comprehensive picture of the state insurance resolution regime.** While NAIC has played an important role in promoting uniformity, state-based resolution regimes vary in their scope and content. This review is based upon an analysis of NAIC model laws and the legislation of two key jurisdictions (New York and New Jersey), as well as discussions with NAIC staff, and representatives of the state insurance departments of New York, New Jersey, California, Nebraska, Connecticut, Pennsylvania and Texas. On this basis, the mission has sought to develop an understanding of general characteristics and approaches to insurance resolution across states and to draw broad conclusions. However, such conclusions need to be viewed against this background.

40. In undertaking the review of the insurance resolution regime, the team looked for specific guidance in the current draft of the AM and the insurance annex to the KAs. The Key Attributes envisage a system in which an administrative authority, in the interest of financial stability, will be vested with broad powers to act quickly to resolve any financial institution that could be systemically important or critical at failure. While discussions continue at the international level on effective resolution strategies for insurance entities, the AM broadly requires the same tools—which can be applied with same speed and flexibility—for systemically important insurance as well as

banking entities.³⁹ With respect to the timelines required for resolution, the AM acknowledges that “it is not necessarily inconsistent with the KA if the resolution regime makes provision for a court order or confirmation for the exercise of resolution powers to be effective” but notes that “it is important to ensure that any requirement for court approval does not impede rapid intervention and the ability to achieve the objectives of resolution.” As will be discussed below, the time-lines required for court approval in the U.S. insurance resolution context may not, in all cases, enable the resolution authorities to achieve the “rapid intervention” envisaged under the KA. While extended timeframes may be appropriate for the exercise of some resolution powers (such as policy transfer and run off), they may be insufficient for other resolution powers that need to be applied more urgently e.g., the transfer of qualified financial contracts (QFCs) of systemic entities. Indeed, the KA and the AM only recognize the need for the application of longer timeframes for policy transfer and run-off; otherwise they assume that same timeframes should apply to the application of resolution powers to systemic insurance companies and banks. The description and analysis of the resolution powers set out below needs to be read against this background and the requirements of the current version of the AM.

41. The challenges involved in applying the draft AM to insurance companies should be noted. It remains a subject of debate as to what degree the KA and the AM may need further modification to address the specific features of insurance companies.⁴⁰ For example, it is not clear whether all the resolution powers envisaged in KA 3 (e.g., asset management companies) are necessary for insurance resolutions, or whether all of the objectives of resolution envisaged in KA 2 are appropriate in the context of insurance resolution. These are questions which may require further discussion within the international community.

³⁹ The methodology only acknowledges the need for longer timelines in an insurance resolution to effect a portfolio transfer or a run off.

⁴⁰ Including by the FSB’s Cross-border Crisis Management Group for Insurers.

| Table 1. Detailed Report | |
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| 1. Scope | |
| KA1.1 | <p>Any financial institution that could be systemically significant or critical if it fails should be subject to a resolution regime that has the attributes set out in the Key Attributes. The regime should be clear and transparent as to the financial institutions (hereinafter “firms”) within its scope. It should extend to:</p> <ul style="list-style-type: none"> (i) holding companies of a firm; (ii) non-regulated operational entities within a financial group or conglomerate that are significant to the business of the group or conglomerate; and (iii) branches of foreign firms. |
| KA1.3 | <p>The resolution regime should require that at least all domestically incorporated global SIFIs (“G-SIFIs”):</p> <ul style="list-style-type: none"> (i) have in place a recovery and resolution plan (“RRP”), including a group resolution plan, containing all elements set out in Annex III; (ii) are subject to regular resolvability assessments; and (iii) are the subject of institution-specific cross-border cooperation agreements. |
| Essential criteria | |
| EC1.1 | <p>The scope of application of the resolution regime and the circumstances in which it applies are clearly defined in the legal framework. Any financial institution that could be systemically significant or critical in the event of failure is subject to a resolution regime.</p> |
| Description and findings re EC1.1 | <p>DFA. The legal framework defines the scope of application of the resolution regime for systemic financial companies, and the circumstances in which it applies, under Title II of the DFA. The definition of financial companies encompasses: (i) bank holding companies; (ii) non bank financial companies supervised by the Federal Reserve Board under Title I of the DFA; (iii) companies predominantly engaged in activities that are financial in nature or incidental thereto, as determined by Federal Reserve Board; and (iv) subsidiaries of companies referred under (i) through (iii) above, other than insured depository institutions or insurance companies, predominantly engaged in activities that are financial in nature or incidental thereto, as determined by Federal Reserve Board.⁴¹</p> <p>The circumstances in which the resolution regime for systemic financial companies applies are also set forth under Title II and are linked to the systemic importance of such companies in the event of failure.⁴² In particular, the resolution regime under Title II applies to financial companies for which a systemic risk determination has been made by the Treasury Secretary that, among other things: the company satisfies the definition of a financial company; such financial company is in default or in danger of default; no viable private sector alternative is available to prevent the default of the financial company; its failure and resolution under otherwise applicable federal or state law would have serious adverse effects on financial stability in the U.S.; and any exercise of the orderly liquidation authority would avoid or mitigate such adverse effects.</p> <p>Such determination is made by the Treasury Secretary in consultation with the President, upon a recommendation made by the FDIC and the Federal Reserve Board (either on their own initiative</p> |

⁴¹ See DFA Section 201(a)(11).

⁴² DFA Section 203.

or at the request of the Treasury Secretary, and subject to what is noted below with respect to insurance companies). Following such determination, and subject to judicial review by the U.S. District Court for the District of Columbia, the FDIC is appointed receiver for the financial company (the “covered financial company”) and can apply the resolution powers under Title II.⁴³ See also below description and findings for Key Attribute 3, and particularly EC 3.1).

When the FDIC has been appointed as a receiver for a financial company under Title II, it may also appoint itself as receiver for a “covered subsidiary” (i.e. a subsidiary of a covered financial company other than an insured depository institution, an insurance company or a covered broker-dealer), upon a joint determination by the FDIC and the Treasury Secretary based on financial stability grounds.⁴⁴ The FDIC can exercise in respect of such subsidiary all powers and rights that it has with respect to a covered financial company under Title II.

Specific issues arise with respect to the resolution of insurance companies under DFA. While holding companies of insurance groups fall within the definition of “financial company” and can be subjected to the resolution regime for systemic financial companies set out under Title II of DFA as described above, the resolution regime for insurance companies under Title II differs from that applicable to other types of companies. In particular,

- A recommendation to treat an insurance company as a “covered financial company” is made by the Director of the Federal Insurance Office (as opposed to the FDIC) and the Board of Governors, at the request of the Secretary or on their own initiative.
- An insurance company that is a “covered financial company” will be subjected to rehabilitation or liquidation under applicable state law rather than the resolution regime specified for other types of financial companies under Title II. State resolution law will also apply to any subsidiary or affiliate of the insurance company that is itself an insurance company.

Accordingly, the resolution of different parts of a systemically important insurance group may be conducted under different resolution regimes: if the holding company is found to be a “covered financial company,” it may be resolved in accordance with the special resolution regime under Title II while any insurance company within the group will be resolved under applicable state resolution law if it enters resolution. To the extent that the resolution involves multiple insurance company subsidiaries incorporated in different states, the relevant state resolution frameworks will be implicated and all relevant state Commissioners will be involved.

Banking. The scope of application of the resolution regime for insured depository institutions is defined under the FDI Act, which provides for the appointment of the FDIC as receiver for Federal and state insured depository institutions on certain grounds.⁴⁵ Insured depository institutions are in turn defined to include any bank or savings association, the deposits of which are insured by the FDIC.⁴⁶ The grounds for the appointment of the FDIC as a receiver, defining the circumstances in which the U.S. resolution regime for insured depository institutions applies, do not necessarily entail that such institutions be systemic or critical in the event of failure.

State Insurance. State insurance receivership laws generally provide for the conduct of

⁴³ DFA Section 202(a).

⁴⁴ DFA Sections 210(a)(1)(E) and 201(a)(9).

⁴⁵ FDI Act, 12 U.S.C. § 1821(c)(5). The FDIC may also appoint itself as receiver of an insured depository institution under the FDI Act (12 U.S.C. § 1821 (c) (10).

⁴⁶ FDI Act, 12 U.S.C. § 1813(a).

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| | <p>proceedings for conservatorship, rehabilitation, or liquidation of the relevant insurance company. The proceedings are commenced and carried out by the relevant state insurance commissioner with state court approval. These proceedings are discussed in greater detail in the KAs below.</p> <p>Findings. With respect to the bank resolution regime, the scope of application of the resolution regime and the circumstances in which it applies are clearly defined under both the DFA and the FDI Act.</p> <p>Several unanswered questions arise from the treatment of insurance companies that are “covered financial companies” under Title II, and the relationship between Title II and state insurance resolution law. First, where an insurance company is determined to be a covered financial company⁴⁷ under Title II, it is not clear whether state resolution proceedings may commence immediately after the determination or only when the company has also crossed the relevant threshold under state law for the commencement of receivership proceedings. Second, it is not clear whether the state receivership proceeding would only need to be conducted in accordance with the objectives for receivership under state law or whether the objectives for orderly liquidation under DFA would also apply. Third, where the state commissioner fails to take the “appropriate judicial action” within 60 days of a systemic risk determination, the precise role of the FDIC in the exercise of the “backup authority” under Section 203 (e)(3) is unclear: while the FDIC, in these circumstances, “shall have the authority” to stand in the place of the relevant regulatory agency and to file the relevant judicial action, it is not clear whether the FDIC would be limited to initiating the proceeding (with the relevant state authority then taking over conduct) or whether it would assume conduct of the proceeding through to its conclusion.</p> <p>The issues described above are particularly complex and remain unresolved. It is recommended that DFA be amended to subject systemically important insurance companies to the same resolution regime applicable to other covered financial companies. (See also recommendation in EC 2.1).</p> |
| <p>EC1.2</p> | <p>The scope of the resolution regime covers the following entities located within the jurisdiction:</p> <ul style="list-style-type: none"> (i) holding companies of firms; (ii) non-regulated operational entities within a financial group or conglomerate that are significant to the business or continuity of the firm’s critical operations; and (iii) domestic branches of foreign firms. |
| <p>Description and findings re EC1.2</p> | <p>DFA. The definition of “financial company” set out in the DFA, to which the resolution regime under Title II applies subject to a systemic risk determination by the Treasury Secretary, includes bank holding companies⁴⁸, nonbank financial companies supervised by the FRB, as determined by the FSOC under Section 113 of the DFA and companies predominantly engaged in activities that the Federal Reserve Board has determined are financial in nature or incidental thereto. Such definition therefore encompasses, but at the same time it goes beyond, the perimeter of non bank financial companies subject to the above mentioned determination by the FSOC. In other words, a financial company does not need to be subject to a FSOC determination under Section 113 of the DFA in order for a resolution proceeding to be commenced for it under Title II. Moreover, the second and the third category permit the inclusion of insurance holding companies within the scope of the DFA resolution regime. A company can qualify as engaged in activities that are financial in nature or incidental thereto, if at least 85 percent of its total consolidated revenues are</p> |

⁴⁷ DFA Section 201(a)(8).

⁴⁸ These are in turn defined under section 2(a) of the Bank Holding Company Act.

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| | <p>derived, directly or indirectly, from financial activities. In turn, financial activities include “insuring, guaranteeing, or indemnifying against loss, harm, damage, illness, disability, or death, or providing and issuing annuities.”⁴⁹</p> <p>Title II may also apply to certain subsidiaries of financial companies predominantly engaged in activities that are financial in nature or incidental thereto, subject to a systemic risk determination. In addition, when the FDIC has been appointed as a receiver for a financial company under Title II, it may appoint itself—through a joint determination with the Treasury Secretary—as receiver for a subsidiary (other than an insured depository institution, an insurance company or a broker-dealer) of such company. Entities that are subsidiaries and are not regulated operational companies (e.g., IT companies) might in principle be captured by this provision of the DFA, if the relevant grounds are met (e.g., default or danger of default of the entity, and the appointment would mitigate the risk to U.S. financial stability). Moreover, upon commencement of an orderly liquidation under Title II the FDIC takes over the assets of and operates the covered financial company with all the powers of the members or shareholders, the directors, and the officers of the company, and conducts all business. This may allow the FDIC to operate the business of the subsidiaries—including non-operational entities—controlled by the covered financial companies.</p> <p>Banking. The scope of application of the resolution regime under the FDI Act includes insured depository institutions. With respect to non-regulated operational entities, the same considerations made above apply with respect to the FDI Act, as the FDIC is authorized to take over the assets and business of IDIs.</p> <p>Domestic branches of foreign banks that are federally licensed are resolved under Federal law, and specifically under the regime set forth by the IBA. State licensed branches are resolved under applicable state laws. As examined below in the description and findings for Key Attribute 7, and particularly EC 7.4, certain shortcomings characterize these regimes as liquidation (rather than resolution) oriented and may not allow to achieve a cooperative solution in a cross-border resolution.</p> <p>As of December 19, 1991, foreign firms may not establish insured branches in the U.S. However, insured branches operating as of that date were permitted to continue operating—52 branches were grandfathered as of that date, and the number of insured branches is currently 10. These insured branches are resolved by the FDIC under the FDI Act.⁵⁰</p> <p>State Insurance. Under State receivership law, where an insurance company has been placed into receivership, an affiliate of the company that is not placed into receivership can be subject to the jurisdiction of the receivership court in limited circumstances. The court may enter orders to ensure that the affiliate does not usurp property of the receivership or otherwise interfere with the receivership. However, it would not appear open to the court to exercise resolution powers with respect to the entity as it is legally separate from the parent. It would generally be open to the receiver, by virtue of its control of the subsidiary, to ensure that essential services continue to be provided to the parent in receivership.</p> <p>The resolution of U.S. branches of foreign insurance companies is a matter of State law. Generally, such branches are liquidated as if they were separate legal entities with the proceeds of liquidation used to satisfy the claims of creditors to the branch. (See KA 7 below).</p> |
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⁴⁹ 12 C.F.R. § 380.8. Financial activities, in turn, include “insuring, guaranteeing, or indemnifying against loss, harm, damage, illness, disability, or death, or providing and issuing annuities”.

⁵⁰ FDI Act, 12 U.S.C. § 1821(c).

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| | <p>Findings. The U.S. resolution regime covers a broad spectrum of entities. However, non-regulated operational entities that are not predominantly engaged in activities that are financial in nature might only be covered by the resolution regime through the ownership link with the covered financial companies, covered subsidiaries, and IDIs that are subject to resolution under Title II or the FDI Act. Similar conclusions are valid under state insurance laws with respect to subsidiaries of insurance companies.</p> <p>Such an ownership link may not always exist (for instance, in case of a company under joint control such as under joint venture agreements) or be operationalized (e.g., when a controlled company is itself subject to an insolvency proceeding, with the bankruptcy trustee having to respond to a different set of duties). In these cases, the resolution regime would not cover non-regulated operational entities. (See also recommendations made under 3.4.) Lastly, the regime for domestic branches of foreign firms is liquidation (rather than resolution) oriented.</p> |
| <p>Assessment of KA1</p> | |
| <p>Comments</p> | <p>The U.S. legal framework defines multiple resolution regimes that could potentially be applied to financial institutions that could be systemically significant or critical in the event of failure, including the DFA, the FDI Act, the IBA and state banking laws (with respect to state-licensed branches of foreign banks), and state insurance receivership laws. As further described in the KA that follow, of the various regimes, the DFA and the FDI Act are most closely aligned with the KA. For these regimes, the scope of application of the resolution regime and the circumstances in which it applies are generally clear, except that certain non-regulated operational entities may not be covered and the relationship between DFA Title II and state insurance resolution law is unclear. To ensure that all financial institutions that could be systemically significant or critical in the event of failure, can be resolved in accordance with a framework that is consistent with the KA, it is recommended that the DFA be amended so that systemically important insurance companies and U.S. branches of foreign banks are subject to a Title II resolution regime similar to that applicable to any other “covered financial companies”. For branches, this should be made in a manner that takes into account the specificities of branches, which are not legal entities, and the need to ensure coordination with foreign resolution authorities in line with KA 7.</p> |
| <p style="text-align: center;">2. Resolution Authority</p> | |
| <p>KA2.1</p> <p>KA2.2</p> <p>KA2.3</p> | <p>Each jurisdiction should have a designated administrative authority or authorities responsible for exercising the resolution powers over firms within the scope of the resolution regime (“resolution authority”). Where there are multiple resolution authorities within a jurisdiction their respective mandates, roles and responsibilities should be clearly defined and coordinated.</p> <p>Where different resolution authorities are in charge of resolving entities of the same group within a single jurisdiction, the resolution regime of that jurisdiction should identify a lead authority that coordinates the resolution of the legal entities within that jurisdiction.</p> <p>As part of its statutory objectives and functions, and where appropriate in coordination with other authorities, the resolution authority should:</p> <ul style="list-style-type: none"> (i) pursue financial stability and ensure continuity of systemically important financial services, and payment, clearing and settlement functions; (ii) protect, where applicable and in coordination with the relevant insurance schemes and arrangements, such depositors, insurance policy holders and investors as are covered by such schemes and arrangements; (iii) avoid unnecessary destruction of value and seek to minimize the overall costs of resolution in home and host jurisdictions and losses to creditors, where that is consistent with the other statutory objectives; and |

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| | (iv) duly consider the potential impact of its resolution actions on financial stability in other jurisdictions. |
| KA2.4 | The resolution authority should have the authority to enter into agreements with resolution authorities of other jurisdictions. |
| KA2.5 | The resolution authority should have operational independence consistent with its statutory responsibilities, transparent processes, sound governance and adequate resources and be subject to rigorous evaluation and accountability mechanisms to assess the effectiveness of any resolution measures. It should have the expertise, resources and the operational capacity to implement resolution measures with respect to large and complex firms. |
| KA2.6 | The resolution authority and its staff should be protected against liability for actions taken and omissions made while discharging their duties in the exercise of resolution powers in good faith, including actions in support of foreign resolution proceedings. |
| KA2.7 | The resolution authority should have unimpeded access to firms where that is material for the purposes of resolution planning and the preparation and implementation of resolution measures. |
| Essential criteria | |
| EC2.1 | The legal framework clearly identifies one or more resolution authorities and provides it or them with a clear mandate. Where there are multiple resolution authorities, the resolution regime provides for the identification of a lead authority; sets out clear arrangements to coordinate the resolution of affiliated legal entities within that jurisdiction; and provides for a clear allocation of objectives, functions and powers of those authorities. |
| Description and findings re EC2.1 | <p>DFA. Title II sets out a multi-step process to activate the resolution regime provided therein, involving several authorities and leading to the appointment by the Treasury Secretary of the FDIC as a receiver for a covered financial company.⁵¹ Each of the authorities and agencies involved in such process acts according to its statutory mandate, as well as based on criteria prescribed by Title II (e.g., financial stability considerations).</p> <p>Title II aims to provide the necessary authority to liquidate failing financial companies that pose a significant risk to the financial stability of the U.S. in a manner that mitigates such risk and minimizes moral hazard, so that, among other things, creditors and shareholders will bear the losses of the financial company, and management responsible for the condition of the financial company will not be retained.⁵²</p> <p>The procedures and division of responsibilities between relevant authorities in the resolution of an insurance group under Title II have not yet been clearly defined and are subject to a significant degree of uncertainty. While it is possible, if the necessary conditions are met, for the FDIC to intervene at the level of a holding company of an insurance group under Title II, the resolution of any insurance company itself would be conducted under State law. However, where the State commissioner fails to take the “appropriate judicial action” within 60 days of a systemic risk determination, the FDIC “shall have the authority” to stand in the place of the relevant regulatory agency and to file the relevant judicial action.</p> <p>The Federal and State authorities have not yet clarified, in a concerted manner, the precise roles that they would play in this process. First (as noted in EC 1.1), in circumstances where the FDIC would exercise its “backup authority” under Title II and initiate resolution proceedings against a “covered” insurance company, it is not clear whether the FDIC would only initiate the proceeding</p> |

⁵¹ See also description and findings under EC1.1 and for Key Attribute 3.

⁵² DFA Section 204(a).

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| <p>(afterwards stepping aside for the relevant State commissioner to conduct the proceeding) or whether it would take the place of the relevant State commissioner for the purposes of conducting the entire proceeding. More generally, the Federal and State authorities have not yet agreed procedures outlining cooperation between the FDIC, other Federal agencies and State commissioners in the period before and within the 60 day window following the determination by the Treasury Secretary with respect to a covered insurance company. Moreover, the Federal and State authorities are still in the process of discussing the procedures that would apply to ensure effective cooperation in circumstances where the FDIC is engaging in a Title II resolution of an insurance holding company and/or its covered subsidiaries where the relevant State commissioners may be engaged in the resolution of insurance companies within the group.</p> <p>To deal with these practical issues, the Dodd-Frank Receivership Implementation Working Group of the Receivership & Insolvency (E) Task Force of NAIC has laid out a possible framework for state implementation of the receivership under DFA, which is reflected in the Guideline for Implementation of State Orderly Liquidation Authority (MDL#1700). While these procedures have not yet been agreed or implemented at the State level, they contemplate an approach under which the commissioner may file a petition for an order of resolution upon certain grounds, including upon determination by the Secretary of Treasury that the insurance company is a financial company satisfying the requirements of such definition under DFA, with a requirement for an expedited (i.e., 24 hour) hearing.</p> <p>It should be noted that the FDIC, as a receiver, is required to consult with the primary financial regulatory agencies (such as the state commissioner with respect to insurance companies) of the covered financial company and its subsidiaries for the purposes of ensuring an orderly liquidation of the covered financial company and coordinate with respect to the treatment or resolution, as the case may be, of such subsidiaries.⁵³ Aside from the issues noted above with respect to insurance group, coordination in the resolution of affiliated legal entities may be facilitated by the FDIC authority to act as the receiver for the covered financial company as well as, subject to certain circumstances, for subsidiaries of covered financial companies.</p> <p>Banking. Under the FDI Act, the FDIC is the resolution authority for all insured depository institutions, including systemically important ones. The FDIC was established to insure the deposits of all banks and savings associations entitled to the benefits of insurance.</p> <p>As regards branches of foreign banking organizations, in case of a state licensed branch the state regulator will appoint a receiver. In case of a federal licensed branch, the receiver will be appointed by the OCC in accordance with Federal law.</p> <p>State Insurance. The state insurance resolution regime designates the commissioner as receiver who takes possession of the insurer in resolution.</p> <p>State insurance resolution law gives the relevant state commissioner the authority to initiate and conduct receivership proceedings respecting any insurance company “domiciled” in its jurisdiction. In such a proceeding, the state commissioner will marshal the assets of the insurer wherever they are located and use them for the purposes of restructuring the company or distributing the proceeds to policy holders and, to the extent proceeds remain, to other associations and funds. Arrangements are in place to ensure coordination with and between state guaranty associations and policy guaranty funds through the coordinating role played by the National Organization of Life and Health Insurance Guaranty Associations (NOLHGA) and the National Conference of Insurance Guaranty Funds (“NCIGF) respectively.</p> |
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⁵³ DFA Sections 204 (c).

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| | <p>Arrangements are also in place for coordination between state commissioners in the event of an interstate receivership, although the rules governing such receiverships at the state level are, to some degree, inconsistent between states. Under these arrangements, the principal “domiciliary” receivership proceeding will be conducted in the state of the company’s domicile, while “ancillary” proceedings may be conducted in other states subject to certain conditions. The Insurer Receivership Model Act (IRMA, 2005) provides that any receivership order granted by the court in the domiciliary state will immediately be given full faith and credit in any other state. It precludes commissioners in other states from commencing ancillary proceedings without the consent of the domiciliary receiver and effectively requires that any such proceedings be conducted in a manner that supports the domiciliary receivership. Earlier model laws which still apply in many states provide a somewhat less complete framework and distinguish between ancillary proceedings launched against insurers that are domiciled in “reciprocal” or “nonreciprocal” states. While ancillary proceedings related to receiverships in reciprocal states are generally required to support the domiciliary proceeding, greater flexibility is provided with respect to proceedings involving insurers in non-reciprocal states. Moreover, there have been cases where domiciliary receivers have encountered difficulties ensuring that orders (e.g., stays on execution) of the domiciliary receivership court are enforced in other states or that ancillary proceedings are conducted in a manner that fully supports the domiciliary receivership.</p> <p>Findings. The U.S. legal framework provides for a number of detailed provisions that identify the responsibilities of the various U.S. authorities in the resolution process under Title II, and vest the FDIC with authority as a receiver. The authorities have been working on the “three key process”, detailing their roles and interaction in the commencement of a Title II proceeding. While the role of the FDIC as resolution authority is clearly defined in line with EC 2.1, , it is recommended that the procedural, internal rules guiding the interaction among the various U.S. authorities involved in the resolution process be finalized.</p> <p>The procedures and division of responsibilities between relevant authorities in the resolution of an insurance group under Title II have not yet been clearly defined and are subject to a significant degree of uncertainty. Without prejudice to the findings under KA 1, it is recommended that the Federal and state authorities clarify the roles that they would play in this process.</p> <p>Under the state insurance resolution regime, the responsibilities of the commissioner as receiver and of the receivership court are clearly defined, although there is a small risk that the actions of a domiciliary receiver may not be supported by commissioners in all states in which the insurer did business.</p> |
| <p>EC2.2</p> | <p>The statutory objectives and functions of the resolution authority include those set out in KA 2.3, as applicable to the sectoral responsibilities of the authority. Where the exercise of resolution powers requires court involvement, the objectives of that involvement are aligned with the statutory objectives and functions set out in KA 2.3.</p> |
| <p>Description and findings re EC2.2</p> | <p>DFA. In taking its action under Title II, the FDIC shall:</p> <ul style="list-style-type: none"> • determine that such action is necessary for purposes of the financial stability of the U.S., and not for the purpose of preserving the covered financial company; • ensure that the shareholders of a covered financial company do not receive payment until after all other claims and the Orderly Liquidation Fund are fully paid; • ensure that unsecured creditors bear losses in accordance with the priority of claim provisions defined under Title II; • ensure that management responsible for the failed condition of the covered financial company is removed; |

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| <ul style="list-style-type: none"> • ensure that the members of the board of directors (or body performing similar functions) responsible for the failed condition of the covered financial company are removed; and • not take an equity interest in or become a shareholder of any covered financial company or any covered subsidiary.⁵⁴ <p>The Dodd-Frank Act prescribes that no taxpayer funds shall be used to prevent the liquidation of any financial company and that taxpayers shall bear no losses from the exercise of any authority under Title II. In exercising its authority, the FDIC shall, to the greatest extent practicable, maximize the net present value return from the sale or disposition of any asset, minimize the amount of any loss realized in the resolution of cases, and mitigate the potential for serious adverse effects to the financial system.</p> <p>Continuity of systemically important financial services, as well as payment, clearing and settlement functions, may be ensured by the FDIC succeeding to all rights, titles, powers, and privileges of the covered financial company, performing all functions of such company.⁵⁵ In this respect, the FDIC can arrange for the transfer of the entity's QFCs, establish a bridge institution, and allow parties to netting contracts to exercise their rights under those contracts.⁵⁶ As a receiver, the FDIC is authorized to make funding available to the receivership for the orderly liquidation of the covered financial company, which may in principle include funds for the continuation of operations, such as payment, clearing, and settlement obligations.⁵⁷</p> <p>The FDIC shall coordinate to the maximum extent possible with appropriate foreign regulatory authorities regarding the resolution of any failed financial company that has any assets or operations in a country other than the U.S.</p> <p>The appointment by the Treasury Secretary of the FDIC as a receiver under Title II is subject to review by the U.S. District Court for the District of Columbia, if the board of directors of the financial company does not consent or acquiesces to such appointment. The court shall decide, on a strictly confidential basis, whether the determination made by the Treasury Secretary that the company is a financial company and is in default or in danger of default is arbitrary and capricious. If the court does not make a determination within 24 hours of receipt of the petition, liquidation under Title II shall automatically commence.</p> <p>With respect to the resolution of an insurance company under the FDIC back-up authority, it is not clear whether the state receivership proceeding would only need to be conducted in accordance with the objectives for receivership under state law or whether the objectives for orderly liquidation under DFA would also apply (see EC 1.1).</p> <p>Banking. The FDIC may not exercise its authority to use certain resolution powers under the FDI Act in connection with an IDI, unless it determines that (i) the exercise of such authority is necessary to meet the obligation of the FDIC to provide insurance coverage for the insured deposits in such institution; and (ii) the total amount of the expenditures by the FDIC and</p> |
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⁵⁴ DFA Section 206.

⁵⁵ DFA Section 210(a)(1).

⁵⁶ See DFA Section 210(c)(9) (with respect to the transfer of qualified financial contracts); Section 210(h) (with respect to bridge institutions); and Section 210(c)(8)(A)(iii) (with respect to netting contracts).

⁵⁷ DFA Section 204(d).

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| | <p>obligations incurred by the FDIC in connection with the exercise of any such authority is the least costly to the deposit insurance fund of all possible methods for meeting the FDIC's obligations.⁵⁸</p> <p>Meeting this least cost test is not required, and the FDIC may take other action or provide assistance for the purposes of winding up an insured depository institution,⁵⁹ if, upon written recommendation of the FDIC and the Federal Reserve Board, the Treasury Secretary determines that (i) compliance with the least cost test would have serious adverse effects on economic conditions or financial stability in the U.S., and (ii) such action or assistance would avoid or mitigate such adverse effects.</p> <p>The FDIC shall conduct its operations as receiver in a manner that, among other things, (i) maximizes the net present value return from the sale or disposition of the assets of the failed IDI; and (ii) minimizes the amount of loss realized in the resolution of cases.⁶⁰</p> <p>The FDIC maintains and administers the deposit insurance fund, which shall not be used to benefit any shareholder or affiliate of any IDI for which the FDIC has been appointed receiver. Payment of insured deposits shall be made by the FDIC as soon as possible after liquidation or winding up of an IDI, either in cash or by making available to each depositor a transferred deposit in another or in a new IDI.⁶¹</p> <p>The FDIC has powers analogous to those granted under Title II, noted above, aimed at ensuring continuity of systemically important financial services, payment, clearing and settlement functions, by succeeding to all rights, titles, powers and privileges of the IDI, transferring any asset or liability of the failed IDI, collecting all obligations and moneys due to the IDI, ensuring that the failed IDI's shareholders do not receive payment until all other claims have been paid, transferring QFCs, and organizing bridge depository institutions.⁶² Once appointed as receiver of a failed IDI, the FDIC is not subject to the direction of any other agency or department of the United States or any state in the exercise of its rights, powers, and privileges.⁶³</p> <p>State Insurance. The overarching statutory objective of the resolution authority under the state insurance resolution law is to protect policyholders, creditors and general public. The protection of the business of insurance is seen to be a matter of vital public interest and concern.</p> <p>The objectives and functions of state insurance resolution regimes do not appear to focus, either explicitly or implicitly, on the protection of financial stability more broadly or on the preservation of critical functions except to the extent that these concepts are encompassed within the protection of policyholders, creditors or the public.</p> <p>Avoiding unnecessary destruction of value and seeking to minimize the overall costs of resolution as well as losses to creditors are within the scope of the legislative objectives.⁶⁴ State resolution frameworks do not appear to require or contemplate the resolution authority giving due</p> |
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⁵⁸ FDI Act, 12 USC. § 1823(c)(4).

⁵⁹ Title XI of the DFA curtailed the systemic risk exception (SRE) authority of the FDIC. This authority can now only be used for IDIs placed into receivership and wound down and not used for open bank assistance.

⁶⁰ FDI Act, 12 USC. § 1821(d)(13)(E).

⁶¹ FDI Act, 12 USC. § 1821(a)(4) and (f)(1).

⁶² FDI Act, 12 USC. § 1821(d)(2); FDI Act, 12 USC. § 1821(e)(9); FDI Act, 12 USC. § 1821(n).

⁶³ FDI Act, 12 U.S.C. § 1821 (c) (2) (C) and (c) (3) (C).

⁶⁴ See IRMA Section 101 E (2)(3)(4)(5).

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| | <p>consideration to the impact of its resolution measures on financial stability in other jurisdictions.</p> <p>Findings. The statutory objectives and functions of the FDIC as resolution authority are broadly in line with those in KA 2.3, in that, as appropriate under Title II and the FDIC Act, they entail the preservation of financial stability, the protection of depositors, and the minimization of losses in resolution. Furthermore, under the DFA, the FDIC as resolution authority is required to coordinate to the maximum extent possible with appropriate foreign regulatory authorities regarding the resolution of any financial failed financial company.</p> <p>In particular, Title II and the FDI Act provide for statutory objectives and responsibilities of the FDIC as resolution authority aimed at ensuring continuity of critical banking and financial services. The FDIC mandate entails the duty to minimize, to the greatest extent possible, losses realized in resolution. The court reviews under a short timeframe whether the Treasury Secretary's determination that the company is a financial company and is in default or in danger of default is arbitrary or capricious, in line with the objectives and functions set out under KA 2.3.</p> <p>The objectives of a Title II proceeding with respect to an insurance company are not clear, given the interaction between the objectives for receivership under state law and those for orderly liquidation under DFA.</p> <p>The objectives and functions of State insurance resolution regimes do not appear to focus on the protection of financial stability more broadly but focus principally on the protection of policy holders.</p> |
| EC2.3 | <p>The resolution authority is, by law and in practice, operationally independent in the performance of its statutory responsibilities. There are arrangements, procedures and safeguards against undue political or industry influence, which include:</p> <ul style="list-style-type: none"> (i) internal governance arrangements which promote sound and independent decision-making; (ii) rules and procedures for the appointment and dismissal of the head of the authority, members of the governing body (where relevant) and senior management; and (iii) rules on conflicts of interest. |
| Description and findings re EC2.3 | <p>DFA and Banking.⁶⁵ The FDIC is an independent regulatory agency of the Federal government.⁶⁶ It is managed by a five-member board of directors, three of whom are appointed by the President of the U.S. with the advice and consent of the U.S. Senate, for a six year term, although one of the appointed directors is designated as Chairman for a five year term. The other members are the Comptroller of the Currency and the Director of the CFPB⁶⁷ each of whom is appointed as Comptroller and Director, respectively, by the President of the United States, with the advice and consent of the U.S. Senate, for a five year term. No more than three members of the Board of Directors shall be from the same political party. The statute does not specify the grounds for removal of the members of the Board of Directors, and there are no precedents in this respect. The FDIC position is that, given that its regulatory functions do not have a purely executive nature; directors may be removed from office only for cause.⁶⁸ By regulation, all employees must meet</p> |

⁶⁵ Given the predominant role of the FDIC, the description and findings for EC 2.3 through EC2.7 discuss jointly both Title II and the FDI Act.

⁶⁶ 44 U.S.C. § 3502(5).

⁶⁷ FDI Act, 12 U.S.C. § 1812 (a) (1) (A) and (B).

⁶⁸ See, e.g., *Humphrey's Executor v. United States*, 295 U.S. 602, 55 S.Ct. 869 (1935).

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| | <p>certain minimum standards for employment with the FDIC.⁶⁹ The dismissal of senior management is subject to certain rules, including in case of breach of ethical standards.</p> <p>With respect to potential conflicts of interest, directors may not hold stock in, or act as an officer or director of, an IDI or bank holding company.⁷⁰ Employees of the FDIC must comply with supplemental standards of ethical conduct, in addition to the ethical standards and financial disclosure regulations applicable to employees of the executive branch.⁷¹</p> <p>General authority to take resolution measures lies with the Board of Directors, which can delegate relevant tasks to FDIC divisions (such as the Division of Resolution & Receiverships).</p> <p>Under Title II, authorities different than the FDIC have a role in commencing the resolution process, and particularly the Treasury Secretary, the Federal Reserve Board and the court. Their role is defined through a number of criteria and safeguards guiding their involvement, and certain checks and balances have been put in place to take into account the risk of inaction.</p> <p>State Insurance. State insurance commissioners can perform their functions in an independent manner and carry out their responsibilities as receivers of insurance companies under the supervision of the court. The offices of state commissioners have in place internal governance arrangements that typically include rules guarding against conflicts of interests. The NAIC has in place an accreditation program with assessment of the insurance supervisory departments in all states helps mitigate the risk of political influence.</p> <p>The qualifications required for the position of state commissioner are, in many cases, specified by statute. These rules typically prohibit the appointment of any person who is connected with the management or control of any insurance company. Moreover, the commissioner as well as the officers and employees of the department are prohibited from having any ownership of, interest in, or any dealings or transactions in any capacity with any insurance company or other financial institution which is licensed or regulated by the department.</p> <p>Findings. The FDIC is subject to rules and procedures aimed at ensuring its operational independence and preserving the autonomy of its heads and staff from industry and political interference. Effective governance arrangements are in place in the offices of State insurance commissioners. The performance of their duties as receivers of insurance companies is subject to judicial oversight.</p> |
| EC2.4 | <p>The resolution authority is accountable through a transparent framework for the discharge of its duties in relation to its statutory responsibilities. This framework includes procedures for reviewing and evaluating actions that the resolution authority takes in carrying out its statutory responsibilities, and the periodic publication of reports on its resolution actions and policies.</p> |
| Description and findings re EC2.4 | <p>DFA and Banking. The FDIC is required to submit to Congress an annual report of its operations, activities, budget, receipts and expenditures for the preceding twelve-month period, including an analysis of the current financial condition of the Deposit Insurance Fund, the purpose, effect, and</p> |

⁶⁹ 12 C.F.R. Part 336.4 and 336.5

⁷⁰ FDI Act, 12 U.S.C. § 1812.

⁷¹ 5 C.F.R. Part 3201.

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| | <p>estimated cost of each resolution action taken for an IDI during the preceding year, and an estimate of the resources needed for the DIF to achieve its statutory purposes.⁷²</p> <p>Before the beginning of each fiscal quarter, the FDIC must provide to the Treasury Secretary a copy of the FDIC's financial operating plans and forecasts. At the end of each fiscal quarter, the FDIC must submit to the Treasury Secretary a copy of the report of the FDIC's financial condition.</p> <p>The FDIC is subject to external review by the Government Accountability Office, through annual audit made by the Comptroller General of the U.S. The FDIC is also subject, like other independent Federal agencies, to Congressional oversight procedures, including providing official responses to formal inquiries and attending hearings as requested by Congress.</p> <p>Specific reporting requirements are established by statute for the FDIC in relation to certain resolution actions undertaken under the FDI Act or Title II of the Dodd-Frank Act.⁷³ The FDIC internal auditor, the Office of the Inspector General, shall perform (i) material loss reviews of the DIF as a result of the failure of an IDI and (ii) semi-annual audits and investigations of the liquidation of any covered financial company under Title II.⁷⁴</p> <p>Within 24 hours of the appointment of the FDIC as receiver for a covered financial company under Title II, the Treasury Secretary shall provide to certain members of Senate and Congress written notice of the recommendations made and determinations reached in connection with the appointment.⁷⁵ The FDIC, as receiver of a covered financial company, shall file a report to certain Committees of Senate and Congress within 60 days of its appointment on the financial condition of the covered financial company and the plan and actions taken by the FDIC to wind down the company.⁷⁶ If the FDIC requires more than three years to resolve a covered financial company under Title II, its Chairperson must certify to certain Senate and Congressional Committees that the continuation of the receivership is necessary to, among other reasons, protect the stability of the financial system of the U.S.</p> <p>The FDIC decisions as receiver with respect to claims are subject to judicial review. Once a claimant has exhausted the administrative claims process, Federal courts have jurisdiction over a <i>de novo</i> review of such claim.⁷⁷</p> <p>State Insurance. The state commissioner both in his capacity as supervisor and in his separate capacity as receiver is subject to accountability mechanisms. Generally, the commissioner is required to make periodic reports to the Governor or state legislature on the operations of his department. In the context of a receivership, however, the principal accountability mechanisms arise from the involvement of the court: a significant majority of the receiver's actions are subject to court approval after notice to interested parties and, in many cases, a hearing. Moreover, the receiver is normally required to make periodic reports on the conduct of the receivership to the court. For example, section 117 of IRMA requires that, within 180 days after the entry of an order of receivership by the receivership court, and at least quarterly thereafter, the receiver must make reports to the court on the conduct of the receivership. Financial reports include, a statement of</p> |
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⁷² See, in general, FDI Act, 12 U.S.C. § 1827.

⁷³ FDI Act, 12 U.S.C. § 1821(d)(15)(A) and (B), and DFA Section 210(a)(16)(A) and (B).

⁷⁴ FDI Act, 12 U.S.C. § 1831o(k), and DFA Section 211(d).

⁷⁵ DFA Section 203(c)(2).

⁷⁶ DFA Section 203(c)(3).

⁷⁷ FDI Act, 12 U.S.C. § 1821(d)(6), and DFA Section 210(a)(4).

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| | <p>the assets and liabilities of the insurer, the changes in those assets and liabilities, and all funds received or disbursed by the receiver during that reporting period. IRMA also requires that guaranty associations involved in a liquidation to file periodic reports to the liquidator, for subsequent inclusion in the liquidator's reports to the receivership court.</p> <p>Findings. The FDIC is subject to numerous, robust accountability requirements, both in terms of external reporting and internal procedures. The accountability regime enables an adequate review of the FDIC actions on an ongoing basis, as well as <i>ex post</i>.</p> <p>State insurance commissioners, as court-appointed receivers, are subject to comprehensive oversight by the court in the performance of their duties, including periodic reporting on the conduct of the receivership.</p> |
| EC2.5 | <p>The resolution authority has adequate human and financial resources or access to such resources, sufficient to enable it to carry out its resolution functions effectively without undermining its independence, both before and during a crisis.</p> |
| Description and findings re EC2.5 | <p>DFA and Banking. The FDIC employs approximately 6,700 people. Further to the enactment of the DFA, the FDIC has revised its internal organization to take account of the new responsibilities under DFA. The Office of Complex Financial Institutions (OCFI) and the Division of Resolutions & Receiverships have, respectively, 79 and 25 positions authorized to address FDIC responsibilities under DFA. A section of the legal division with 27 employees provides primary support to OCFI and other FDIC divisions working on DFA matters. The Division Risk Management Supervision (RMS) has a separate branch, named Complex Financial Institutions, formed to handle FDIC supervisory duties of SIFIs with 110 employees, mostly senior. The FDIC has in place a program for professional training, including on DFA-related matters.</p> <p>The operations of the FDIC acting in its corporate capacity are generally funded by the Deposit Insurance Fund (DIF), which is funded through regular assessments on IDIs. The operations of the FDIC in its capacity as receiver of failed IDIs are funded by the assets of the failed IDI and, if necessary, the DIF;⁷⁸ likewise, the FDIC's operations relating to the resolution of failed financial companies under Title II are funded by the assets of the failed financial company and, if necessary, the Orderly Liquidation Fund. The FDIC is authorized to borrow from the U.S. Treasury if necessary for insurance purposes.⁷⁹ Reasonable implementation expenses of the FDIC incurred as part of its efforts to implement Title II are treated as expenses of the FSOC. In turn, the FSOC's expenses are funded through assessments on bank holding companies with total consolidated assets of \$50 billion or more and nonbank financial companies supervised by the Federal Reserve Board.⁸⁰</p> <p>State Insurance. In ensuring that they have the expertise and financial resources necessary to perform their receivership function, States take a variety of different approaches. Some states do not have specialized internal units within the department of the insurance commissioner, although some do and a few have separate legal entities. Such entities act on the behalf and under the supervision of the commissioner. In many states where the commissioner has few specialized staff, external experts (especially lawyers, accountants and appraisers) are hired on a contractual basis to assist in conducting the receivership.</p> |

⁷⁸ FDI Act, 12 U.S.C. § 1823(d) (1) and (2).

⁷⁹ FDI Act, 12 U.S.C. § 1824(a). The FDIC is also authorized to borrow "on behalf of the Deposit Insurance Fund" from the Federal Financing Bank and from the Federal home loan banks, FDI Act 12 U.S.C. § 1824 (b) and (e).

⁸⁰ DFA Sections 118, 155(d), 210(n)(10) and 210 (o)(1).

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| | <p>The expenses related to the receivership proceedings are funded primarily from the assets of the estate. If guaranty associations are formally involved in the receivership, their expenses are also funded from the assets of the estate as well as by assessments among the other insurers in the particular states.</p> <p>Findings. The FDIC is equipped with the adequate human and financial resources necessary to carry out its functions effectively.</p> <p>The organization and resources of the receiver of an insurance company vary significantly across different states. While these appear to have been adequate to deal with the vast majority of receiverships arising in the United States, it would need to be determined to what degree they would be sufficient to deal with the failure of a systemically important insurer.</p> |
| <p>EC2.6</p> | <p>The legal framework provides legal protection through statute for the resolution authority, its head, members of the governing body and its staff and any agents against liability for actions taken or omissions made while discharging their duties in good faith and acting within the scope of their powers, including actions taken in support of foreign resolution proceedings; including indemnification against any costs of defending any such actions.</p> |
| <p>Description and findings re EC2.6</p> | <p>DFA and Banking. The liability regime for the FDIC and its officials is provided under the Federal Tort Claims Act (FTCA).⁸¹ The FTCA provides for a waiver of sovereign immunity in certain cases involving torts committed by government employees, holding the Government liable if the employee was acting within the scope of his office or employment. While it grants jurisdiction for actions seeking money damages for injury, property loss or death caused by the negligent or wrongful acts or omissions of federal employees, the FTCA contains a number of exceptions, disallowing certain claims. This includes any claim based upon an act or omission of an employee of the Government, exercising due care, in the execution of a statute or regulation or based upon the exercise of a discretionary function, whether or not the discretion involved be abused.</p> <p>The remedy provided under FTCA against federal agencies such as the FDIC, or its officials shall be exclusive of any other civil action or proceeding for money damages by reason of the same subject matter against the employee. Thus, if a tort suit does not lie under the FTCA, the action is barred altogether.</p> <p>A director, member, officer, or employee of the FDIC has no liability under the Securities Act of 1933, with respect to any claim arising out of any act or omission by such person within the scope of such person’s employment in connection with any transaction involving the disposition of assets by the FDIC.⁸²</p> <p>Pursuant to the FDIC’s Indemnification Policy, set forth in Circular 5000.1, the FDIC will indemnify a present or past director, officer or employee of the FDIC against liability and expenses incurred in connection with any claim for wrongful acts in which the person may become involved by reason of being or having been a director, officer or employee.</p> <p>State Insurance. Section 115 alternative 1B of IRMA renders subject persons with official or judicial immunity, immunity from suit and liability arising out of their duties or employment. Alternatively, Section 115 alternative 1C (1) of IRMA entitles the subject persons to indemnification for property damage, property loss, personal injury or other civil liability caused by any alleged act, error or omission. The subject persons may be indemnified from the assets of the insurer, unless it is determined that the alleged act, error or omission of the subject person did not arise</p> |

⁸¹ FTCA, 28 U.S.C. § 2671 *et seq.*

⁸² FDI Act, 12 U.S.C. § 1812(f)(1).

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| | <p>out of their duties, or was caused by intentional or willful and wanton misconduct.</p> <p>These forms of protection were not included in previous NAIC model laws and it would appear that only some states have incorporated these types of protections into their legislative frameworks.</p> <p>Findings. The FDIC enjoys adequate legal protection in line with recommendations set out in EC2.6. The degree of legal protection granted under state insurance resolution regimes varies across states. While some state insurance resolution regimes provide protection for the commissioner as receiver, both personally and in his official capacity, his assistants and contractors (collectively, “subject persons”) against liability for actions taken or omissions made while discharging their duties in good faith and acting within the scope of powers, other states, given receivership proceedings involve state court approval, have not incorporated such protection into their legislation.</p> |
| EC2.7 | <p>Under the legal framework, the resolution authority has unimpeded access to the domestic premises of firms where that is material for the purposes of resolution planning and the preparation and implementation of resolution measures.</p> |
| Description and findings re EC2.7 | <p>DFA and Banking. Access to firms for the purposes of resolution planning may be attained by the FDIC through its special examination authority with respect to any IDI, any affiliate of an IDI, nonbank financial company supervised by the Federal Reserve Board, and any bank holding company with total consolidated assets equal to or greater than \$50 billion.⁸³ The FDIC may exercise this special examination authority with respect to any IDI for which the FDIC is not the primary Federal regulator whenever the FDIC determines that a special examination of any such IDI is necessary to determine the condition of such IDI for insurance purposes. The FDIC coordinates with such IDI’s primary Federal regulator. The exercise of the special examination authority with respect to any nonbank financial company supervised by the Federal Reserve Board or bank holding company with total consolidated assets equal to or greater than \$50 billion is carried out for the purpose of implementing the FDIC’s authority under Title II of the Dodd-Frank Act. However, this is limited to the circumstance that such nonbank financial company or bank holding company is not in a generally sound condition.⁸⁴ When this circumstance is not met the FDIC would not have direct access to such information, but it could still make use of the information sharing mechanisms with the relevant federal regulatory agencies.</p> <p>Upon appointment as receiver, the FDIC succeeds to all rights, titles, powers, and privileges of the covered financial company or IDI, as well as their assets, as the case may be. The FDIC takes over the assets of, and operates, such company or IDI, which enables the FDIC to have access also to domestic premises of the financial company or IDI.⁸⁵</p> <p>State Insurance. Under the state insurance holding company law, the commissioner as state regulator has access to the books, records and other information held by the insurer and its affiliates.</p> <p>For example, under the Insurance Holding Company System Regulatory Act (Model Act or MDL#440, “IHCA”), a model regulation adopted by the NAIC in 2015, the commissioner has the</p> |

⁸³ FDI Act, 12 USC. § 1820(b)(3) and (4).

⁸⁴ *Id* Ibid.

⁸⁵ FDI Act, 12 USC. § 1821(d)(2)(A) and (B), and DFA Section 210(a)(1)(A) and (B).

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| | <p>power to examine an insurer and its affiliates to ascertain the financial condition of each of the insurer group companies and the insurer group as a whole.⁸⁶ Although useful, these provisions do not directly address the question of resolution planning.</p> <p>Findings. The FDIC has unimpeded access to the domestic premises of firms in resolution. Its access to firms in connection with the preparation of a resolution does not encounter impediments for IDIs, but is subject to a significant constraint for non bank financial companies or bank holding companies. These must not be in a generally sound condition in order for the FDIC to be able to exercise its special examination authority. However, the FDIC could, in any event, still make use of the information sharing mechanisms in place with the relevant federal regulatory agencies. With respect to the state insurance resolution regimes, the commissioner has access to information generally regarding insurance group companies, rather than specifically with respect to recovery and resolution planning.</p> |
| Assessment of KA2 | |
| Comments | <p>The mandate of the FDIC, as a key resolution authority, is clearly defined in the legal framework. Its statutory objectives and functions are broadly in line with Key Attribute 2. The FDIC is subject to a robust accountability and transparency framework and benefits from adequate legal protection for actions taken within the scope of its powers. In contrast, the overarching statutory objective of the resolution authority under the state insurance resolution law is to protect policyholders, creditors and general public. The objectives and functions of state insurance resolution regimes do not appear to focus, either explicitly or implicitly, on the protection of financial stability more broadly or on the preservation of critical functions except to the extent that these objectives might be indirectly served by actions taken to protect policyholders. State insurance resolution authorities are subject to accountability and reporting requirements primarily through the role of the court.</p> <p>For the FDIC to effectively perform its role as the resolution authority, appropriate mechanisms for coordination with other agencies involved in resolution will be critical. It is recommended to finalize the procedural rules detailing the interaction between the various federal authorities in relation to the commencement of a Title II proceeding under the “three key process.” With respect to the resolution of an insurance company under Title II, significant uncertainties arise with respect to the allocation of responsibilities between state authorities and the FDIC. This may have repercussions, for instance, on the objectives of a proceeding commenced under the FDIC back-up authority provided in accordance with Title II. Pending implementation of the recommendation in KA 1 to extend the scope of the DFA to cover insurance companies, the authorities are encouraged to clarify the roles and responsibilities between federal and state authorities in the resolution of an insurance group under Title II, including with respect to the triggers, objectives, coordination mechanisms and funding sources.</p> |
| 3. Resolution Powers | |
| KA3.1 | <p>Resolution should be initiated when a firm is no longer viable or likely to be no longer viable, and has no reasonable prospect of becoming so. The resolution regime should provide for timely and early entry into resolution before a firm is balance-sheet insolvent and before all equity has been fully wiped out. There should be clear standards or suitable indicators of non-viability to help guide decisions on whether firms meet the conditions for entry into resolution.</p> |
| KA3.2 | <p>Resolution authorities should have at their disposal a broad range of resolution powers, which should</p> |

⁸⁶ IHCA Section 6 A.

include powers to do the following:

- (i) Remove and replace the senior management and directors and recover monies from responsible persons, including claw-back of variable remuneration;
- (ii) Appoint an administrator to take control of and manage the affected firm with the objective of restoring the firm, or parts of its business, to on-going and sustainable viability;
- (iii) Operate and resolve the firm, including powers to terminate contracts, continue or assign contracts, purchase or sell assets, write down debt and take any other action necessary to restructure or wind down the firm's operations;
- (iv) Ensure continuity of essential services and functions by requiring other companies in the same group to continue to provide essential services to the entity in resolution, any successor or an acquiring entity; ensuring that the residual entity in resolution can temporarily provide such services to a successor or an acquiring entity; or procuring necessary services from unaffiliated third parties;
- (v) Override rights of shareholders of the firm in resolution, including requirements for approval by shareholders of particular transactions, in order to permit a merger, acquisition, sale of substantial business operations, recapitalization or other measures to restructure and dispose of the firm's business or its liabilities and assets;
- (vi) Transfer or sell assets and liabilities, legal rights and obligations, including deposit liabilities and ownership in shares, to a solvent third party, notwithstanding any requirements for consent or novation that would otherwise apply (see Key Attribute 3.3);
- (vii) Establish a temporary bridge institution to take over and continue operating certain critical functions and viable operations of a failed firm (see Key Attribute 3.4);
- (viii) Establish a separate asset management vehicle (for example, as a subsidiary of the distressed firm, an entity with a separate charter, or as a trust or asset management company) and transfer to the vehicle for management and run-down non-performing loans or difficult-to-value assets;
- (ix) Carry out bail-in within resolution as a means to achieve or help achieve continuity of essential functions either (i) by recapitalising the entity hitherto providing these functions that is no longer viable, or, alternatively, (ii) by capitalising a newly established entity or bridge institution to which these functions have been transferred following closure of the non-viable firm (the residual business of which would then be wound up and the firm liquidated) (see Key Attribute 3.5);
- (x) Temporarily stay the exercise of early termination rights that may otherwise be triggered upon entry of a firm into resolution or in connection with the use of resolution powers (see Key Attribute 4.3 and Annex IV);
- (xi) Impose a moratorium with a suspension of payments to unsecured creditors and customers (except for payments and property transfers to central counterparties (CCPs) and those entered into the payment, clearing and settlements systems) and a stay on creditor actions to attach assets or otherwise collect money or property from the firm, while protecting the enforcement of eligible netting and collateral agreements; and
- (xii) Effect the closure and orderly wind-down (liquidation) of the whole or part of a failing firm with timely pay-out or transfer of insured deposits and prompt (for example, within seven days) access to transaction accounts and to segregated client funds).

KA3.3

Resolution authorities should have the power to transfer selected assets and liabilities of the failed firm to a third party institution or to a newly established bridge institution. Any transfer of assets or liabilities should not:

- (i) require the consent of any interested party or creditor to be valid; and
- (ii) constitute a default or termination event in relation to any obligation relating to such assets or

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| | liabilities or under any contract to which the failed firm is a party (see Key Attribute 4.2). |
| KA3.4 | <p>Resolution authorities should have the power to establish one or more bridge institutions to take over and continue operating certain critical functions and viable operations of a failed firm, including:</p> <p>(i) the power to enter into legally enforceable agreements by which the authority transfers, and the bridge institution receives, assets and liabilities of the failed firm as selected by the authority;</p> <p>(ii) the power to establish the terms and conditions under which the bridge institution has the capacity to operate as a going concern, including the manner under which the bridge institution obtains capital or operational financing and other liquidity support; the prudential and other regulatory requirements that apply to the operations of the bridge institution; the selection of management and the manner by which the corporate governance of the bridge institution may be conducted; and the performance by the bridge institution of such other temporary functions as the authority may from time to time prescribe;</p> <p>(iii) the power to reverse, if necessary, asset and liability transfers to a bridge institution subject to appropriate safeguards, such as time restrictions; and</p> <p>(iv) the power to arrange the sale or wind-down of the bridge institution, or the sale of some or all of its assets and liabilities to a purchasing institution, so as best to effect the objectives of the resolution authority.</p> |
| KA3.5 | <p>Powers to carry out bail-in within resolution should enable resolution authorities to:</p> <p>(i) write down in a manner that respects the hierarchy of claims in liquidation (see Key Attribute 5.1) equity or other instruments of ownership of the firm, unsecured and uninsured creditor claims to the extent necessary to absorb the losses; and to</p> <p>(ii) convert into equity or other instruments of ownership of the firm under resolution (or any successor in resolution or the parent company within the same jurisdiction), all or parts of unsecured and uninsured creditor claims in a manner that respects the hierarchy of claims in liquidation;</p> <p>(iii) upon entry into resolution, convert or write-down any contingent convertible or contractual bail-in instruments whose terms had not been triggered prior to entry into resolution and treat the resulting instruments in line with (i) or (ii).</p> |
| KA3.6 | <p>The resolution regime should make it possible to apply bail-in within resolution in conjunction with other resolution powers (for example, removal of problem assets, replacement of senior management and adoption of a new business plan) to ensure the viability of the firm or newly established entity following the implementation of bail-in.</p> |
| KA3.7 | <p>In the case of insurance firms, resolution authorities should also have powers to:</p> <p>(i) undertake a portfolio transfer moving all or part of the insurance business to another insurer without the consent of each and every policy holder; and</p> <p>(ii) discontinue the writing of new business by an insurance firm in resolution while continuing to administer existing contractual policy obligations for in-force business (run-off).</p> |
| KA3.8 | <p>Resolution authorities should have the legal and operational capacity to:</p> <p>(i) apply one or a combination of resolution powers, with resolution actions being either combined or applied sequentially;</p> <p>(ii) apply different types of resolution powers to different parts of the firm's business (for example, retail and commercial banking, trading operations, insurance); and</p> <p>(iii) initiate a wind-down for those operations that, in the particular circumstances, are judged by the authorities to be not critical to the financial system or the economy (see Key Attribute 3.2 xii).</p> |
| KA3.9 | <p>In applying resolution powers to individual components of a financial group located in its jurisdiction,</p> |

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| <p>the resolution authority should take into account the impact on the group as a whole and on financial stability in other affected jurisdictions, and undertake best efforts to avoid taking actions that could reasonably be expected to trigger instability elsewhere in the group or in the financial system.</p> | |
| <p>Essential criteria</p> | |
| <p>EC 3.1</p> | <p>The legal framework includes clear criteria that provide for timely and early entry into resolution before a firm is balance sheet insolvent, when a firm is no longer viable or when it is likely to be no longer viable and, in either case, has no reasonable prospect of return to viability. Adequate arrangements are in place to support the timely determination of non-viability or likely non-viability.</p> |
| <p>Description and findings re EC3.1</p> | <p>DFA. In order for the FDIC to be appointed receiver under Title II, several steps are required. A recommendation must be made by the FRB and the FDIC to place a financial company other than a broker-dealer or insurance company into receivership.⁸⁷ Upon a vote by two thirds of the directors of both the FRB and the FDIC⁸⁸ a written recommendation is delivered to the Treasury Secretary, which amongst other requirements must include:</p> <ul style="list-style-type: none"> • evaluation of whether the financial company is in default or in danger of default; • description of the effect that the default of the financial company would have on financial stability in the U.S.; and • evaluation of why a case under the Bankruptcy Code is not appropriate for the financial company. <p>The Treasury Secretary, in consultation with the U.S. President must determine whether the financial company should be placed into receivership, based (amongst other factors) on whether:</p> <ul style="list-style-type: none"> • the financial company is in default or in danger of default; • the failure of the financial company and its resolution under otherwise applicable federal or state law would have serious adverse effects on financial stability in the U.S.; • no viable private sector alternative is available to prevent the default; • any effect on creditors, counterparties, and shareholders of the financial company and other market participants as a result of actions under Title II is appropriate, given the impact that such actions would have on financial stability in the U.S.; • any exercise of the OLA would avoid or mitigate such adverse effects, taking into account the effectiveness the OLA powers in mitigating (i) potential adverse effects on the financial system, (ii) the cost to the Treasury, and (iii) the potential to increase excessive risk taking on the part of creditors, counterparties, and shareholders in the financial company; and • a Federal regulatory agency has ordered the financial company to convert all of its convertible debt instruments that are subject to the regulatory order. |

⁸⁷ DFA Section 203(a)(1)(A).

⁸⁸ Or a 2/3 vote by the Federal Reserve Board and the SEC in the case of a broker or dealer or a financial company in which the largest domestic subsidiary is a broker or dealer, or a 2/3 vote by the Federal Reserve Board and the approval of the Director of FIO in the case of an insurance company or a financial company in which the largest domestic subsidiary is an insurance company.

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| | <p>Following the Treasury Secretary’s determination to appoint the FDIC as receiver, the Treasury Secretary must notify the financial company. If the financial company’s board of directors consents to the FDIC’s appointment as receiver, the Treasury Secretary immediately appoints the FDIC. In the absence of acquiescence or consent by the board of directors, the U.S. district court for the District of Columbia has a statutorily circumscribed and expedited role in reviewing the appointment of the FDIC as receiver, before the proceeding can commence (see EC 5.5 for further details).</p> <p>Section 203(c)(4) of the Dodd-Frank Act, 12 USC § 5383(c)(4), provides that, for purposes of Title II of the Dodd-Frank Act, a financial company shall be considered to be in default or in danger of default if (A) a case has been, or likely will promptly be, commenced with respect to the financial company under the Bankruptcy Code, (B) the financial company has incurred, or is likely to incur, losses that will deplete all or substantially all of its capital, and there is no reasonable prospect for the company to avoid such depletion, (C) the assets of the financial company are, or are likely to be, less than its obligations to creditors and others, or (D) the financial company is, or is likely to be, unable to pay its obligations (other than those subject to a bona fide dispute) in the normal course of business.⁸⁹ The authorities are developing inter-agency procedures to support a timely determination under the “three keys” process and agree the analysis and data requirements.</p> <p>As noted in EC 1.1, , while the resolution of a holding company of an insurance group would be subject to the regime described above, the resolution regime for an insurance company itself under Title II differs in that: (i) the recommendation to treat an insurance company as a “covered financial company” would be made by the Director of the Federal Insurance Office (as opposed to the FDIC) and the Board of Governors (made by a vote of no fewer than 2/3 of the Board of Governors), at the request of the Secretary or on their own initiative; and (ii) an insurance company that is a “covered financial company” will be subjected to rehabilitation or liquidation under applicable state law. However, it is not clear whether state resolution proceedings could be commenced immediately after the determination or only when the company has also crossed the relevant threshold under state law for the commencement of receivership proceedings (although, as discussed below, it is recognized that the “hazardous financial condition” criteria allows state insurance resolution authorities to commence proceedings at a relatively early stage of an insurance company’s difficulties).</p> <p>Banking. The decision to resolve an insured depository institution is usually made by its federal or state chartering authority. If the chartering authority decides to place the institution into receivership, the FDIC must be appointed receiver.⁹⁰ An IDI may be placed into receivership when a wide range of trigger events are met, including:</p> <ul style="list-style-type: none"> • assets are less than the institution’s obligations; • substantial dissipation of assets due to any violation of any statute or regulation, or any unsafe or unsound practice; • an unsafe or unsound condition to transact business; • any wilful violation of a cease-and-desist order; • any concealment of the institution’s books, papers, records, or assets; • the institution is likely to be unable to pay its obligations or meet its depositors’ |
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⁸⁹ DFA Section 203(c)(4).

⁹⁰ FDI Act 12 USC. § 1821(c).

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| | <p>demands in the normal course of business;</p> <ul style="list-style-type: none"> • the institution has incurred or is likely to incur losses that will deplete all or substantially all of its capital, and there is no reasonable prospect for the institution to become adequately capitalized without Federal assistance; • any violation of any law or regulation, or any unsafe or unsound practice or condition that is likely to cause insolvency or substantial dissipation of assets or earnings, weaken the institution's condition or otherwise seriously prejudice the interests of the institution's depositors or the deposit insurance fund; • the institution, by resolution of its board of directors or its shareholders or members, consents to the appointment; • the institution ceases to be an insured institution; • the institution is undercapitalized under the PCA scheme of 12 USC. § 1831o (defined as failing to meet any required minimum level of capital)⁹¹ and (i) has no reasonable prospect of becoming adequately capitalized; (ii) fails to become adequately capitalized when required to do so under section 1831o; (iii) fails to submit a capital restoration plan acceptable to its Federal supervisor within the time prescribed under section 1831o; or (iv) materially fails to implement a capital restoration plan submitted and accepted under section 1831o; • the institution is critically undercapitalized or otherwise has substantially insufficient capital; and • the institution has been found guilty of a money laundering offense under applicable U.S. law. <p>Under the PCA regime a critically undercapitalized bank (defined as tangible equity less than 2 percent of total assets) must be placed in conservatorship or receivership within 90 days of such a determination, unless the FDIC and appropriate regulators determine that other action would protect the DIF. In practice, the FDIC and the IDI's primary federal supervisor may begin working on preparing to place the IDI into receivership or to look for a healthy institution to purchase the troubled IDI at an early juncture e.g., if an IDI depletes capital slowly over time before it reaches critically undercapitalized. Under certain circumstances the FDIC also has a rarely used authority to appoint itself as receiver, after consultation with but without requiring the consent of the chartering authority of the IDI.⁹²The FDIC has established processes to ensure it has timely access to relevant firm-specific information, including through its statutory special examination authority (see EC 2.7 for further detail) to promptly act in the event of an IDI's distress.</p> <p>State Insurance. State insurance resolution law generally permits the commencement of receivership proceedings at a relatively early stage of an insurance company's difficulties. For example, section 207 of IRMA permits the commencement of such proceedings not only where the insurer is impaired or insolvent but is about to become insolvent, or is in such condition that the "further transaction of business would be hazardous financially to its policyholders, creditors or the public." The NAIC has issued (July 2010) Model Regulations to Define Standards and Commissioner's Authority of Companies Deemed to be in Hazardous Financial Condition (MDL#385). These set out standards which, either singly or a combination of two or more, may be</p> |
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⁹¹ CP 16 of the BCP for the detailed PCA thresholds and restrictions.

⁹² 12 U.S.C. 1821(c)(10).

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| | <p>considered by the commissioner to determine whether the continued operation of insurer might be deemed to be hazardous to its policyholders, creditors or the general public. The standards include:</p> <ul style="list-style-type: none"> a) Adverse findings reported in financial condition and market conduct examination reports, audit reports and actuarial opinions, reports or summaries; b) Whether the insurer has made adequate provision for the anticipated cash flows c) Whether the insurer’s operating loss in the last twelve-month period or any shorter period of time is greater than 50 percent of the insurer’s remaining surplus as regards policyholders in excess of the minimum required; d) Whether the insurer’s operating loss in the last twelve-month period or any shorter period of time, excluding net capital gains, is greater than 20 percent of the insurer’s remaining surplus as regards policyholders in excess of the minimum required; e) When authorized by risk based capital regulations. <p>Findings. The OLA powers can be triggered when a firm is or is “likely to” be balance sheet or cash flow insolvent or has depleted “substantially all of its capital.” Whether resolution would be triggered sufficiently early, in particular before insolvency and when the firm is no longer viable (e.g., because its liquidity or capital is significantly depleted) will depend upon the authorities’ interpretation in practice of these statutory terms. It is recommended that the authorities issue guidance to elaborate on the circumstances, including “suitable indicators of non-viability” (EN 3.1(c)) with illustrative scenarios as examples, that would be taken into consideration in reaching a decision to commence OLA prior to insolvency, in particular with regard to the interpretation of “likely to” and “substantially all.” This would provide more clarity and could more explicitly align with the KA, without overly restraining flexibility needed to deal with the circumstances of any particular case. With respect to insurance companies and as noted in EC 1.1, there is a lack of clarity as to the manner in which the DFA triggers will “mesh” with those provided for under state resolution law.</p> <p>The FDI Act provides a wider range of triggers under which an IDI can be placed into resolution, which along with the mandatory resolution under the PCA regime (see Core Principle (CP) 11 of the BCP assessment) allows for sufficiently early resolution. Under state insurance receivership law, a resolution proceeding may be issued reasonably in advance of an insurer’s insolvency, with detailed triggers available for this purpose although, in all cases, subject to court approval.</p> |
| EC3.2 | <p>The resolution authority, either directly or through the supervisory authority, has powers to remove and replace senior management and directors of the firm in resolution. It or another authority has the power to pursue claims and recover monies, including variable remuneration, from persons whose actions or omissions have caused or materially contributed to the failure of the firm.</p> |
| Description and findings re EC3.2 | <p>DFA. Under Section 210(a)(1)(A) the FDIC as receiver succeeds to all rights, titles, powers, and privileges of the failed firm and of any stockholder, member, officer or director of the firm. As such the FDIC has the power to remove and replace senior management and directors of a firm in resolution, including a bank or insurance holding company. The DFA also introduced a statutory obligation to dismiss managers and directors responsible for the condition of the failed financial company.⁹³</p> |

⁹³ DFA Sections 204(a)(2) and 206(4) and (5).

The FDIC has the power to pursue monetary damages, by commencing a civil judicial action, from directors or officers of a covered financial company whose actions are deemed grossly negligent.⁹⁴ In addition, the FDIC as receiver is authorized to file an action to recoup past “compensation” from current or former senior executives and directors “substantially responsible” for the condition of the failed financial company for a period of two years preceding the failure of the financial company and, in cases of fraud, for an unlimited period of time.⁹⁵ The standard of care for which the FDIC can seek to recoup compensation paid to senior executives and directors is a negligence test i.e., gross negligence is not required. The FDIC will deem a senior executive or director “substantially responsible” for a covered financial company’s failure if that person failed to conduct his or her responsibilities “with the degree of skill and care an ordinarily prudent person in a like position would exercise under similar circumstances.” Compensation includes variable remuneration such as bonuses and incentives.

Banking. FDIC as receiver succeeds to all rights, titles, powers, and privileges of the failed IDI and of any stockholder, member, officer or director of the firm. As such the FDIC has the power to remove and replace senior management and directors. It can also pursue claims and recover monies from directors and officers of an IDI, either by commencing a civil judicial action for monetary damages for gross negligence or any similar conduct or conduct demonstrating a greater disregard of a duty of care (than gross negligence) as defined under state law or by commencing actions for civil money penalties pursuant to the FDIC’s enforcement authority.⁹⁶ Similarly, the OCC also has the authority to take enforcement action such as civil money penalties, prohibition actions, or personal cease and desist actions against an institution affiliated party, including offices and directors that served in the bank before it failed. However, the FDI Act does not provide for powers to recover compensation from current or former senior executives whose actions or omissions have caused or materially contributed to the failure of the firm.

State Insurance. State insurance receivership law generally permits the commissioner to remove and replace senior management of a firm in receivership. For example, Section 402 A of IRMA provides that the commissioner as rehabilitator has all the powers of directors of the directors, officers and managers of the insurer, whose authority is suspended except as re-delegated by the rehabilitator. The rehabilitator may pursue all the appropriate legal remedies on behalf of the insurer if it appears that there has been criminal or tortious conduct, or breach of any contractual or fiduciary obligation detrimental to the insurer by any officer manager, agent, broker, employee, affiliate or other person. Broadly similar provisions exist in the legislative framework of New Jersey and of many other states.

Findings. The authorities have the powers both under the DFA and the FDI Act to remove and replace the senior managers and directors of a firm in resolution. While they also have powers in both the DFA and the FDI Act to pursue monetary damages from directors and officers through civil action, it is recommended to amend the FDI Act to provide similar powers to those in the DFA. Specifically, to recover compensation, including variable remuneration, from those “substantially responsible” for the failure of the firm. Under U.S. state insurance receivership laws the commissioner, as receiver, has the power to remove and replace senior management and directors of the insurer in resolution. Also the commissioner as receiver generally has the power to pursue appropriate legal remedies on behalf of the insurer, including pursuing monetary damages by commencing a civil judicial action from its directors, officers or employees for tortious conduct

⁹⁴ DFA Section 210(f) and 12 CFR 380.7.

⁹⁵ DFA Section 210(s).

⁹⁶ FDI Act 12 USC. §§ 1818(i) and 1821(k).

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| | or the breach of a contractual or fiduciary obligation. |
| EC3.3 | The resolution authority has powers, directly or indirectly through an administrator, to temporarily take control and operate a firm in order to achieve its orderly resolution. This includes powers to restructure or wind down the firm’s operations; terminate, continue or assign contracts; enter into contracts and service agreements to ensure the continuity of essential services and functions; and purchase or sell assets. |
| Description and findings re EC3.3 | <p>DFA: The FDIC as the resolution authority has the power to take control directly and operate a firm to achieve the firm’s orderly resolution. The FDIC as receiver has broad authority to manage the assets and operations of the failed institution in resolution to, among other things, restructure or wind down the failed institution, repudiate contracts, enforce contracts, assign contracts to a bridge financial company or purchasing entity,⁹⁷ enter into contracts, and purchase and sell assets.⁹⁸</p> <p>Banking. The FDIC as receiver of IDIs has similar powers; the DFA clauses were actually based upon those in the FDI Act. In addition, the FDIC has conservator powers which can be used to try and preserve the going concern value of the IDI, for example, by restructuring and returning it to health. The conservator powers differ in several ways from those of receivership e.g., shorter protection is afforded against termination rights (45 days compared to 90 in receivership. These differences are relevant, for example, with regard to the discussion of EC3.7.</p> <p>State Insurance. Many state insurance resolution laws empower the commissioner to obtain a “seizure order,” often on an ex parte basis (e.g., Section 201 of IRMA) where there exist grounds that would justify a court order for formal receivership proceedings and the interests of policyholders, creditors and the public will be endangered by delay. While a seizure order would permit the commissioner to take control of the company, the exercise of more comprehensive resolution powers would require, inter alia, the commencement of receivership proceedings and a court order.</p> <p>The state commissioner, as receiver, is vested by a receivership order with broad powers over the insurer and, subject to the supervision of the court, controls all aspects of the insurer’s operations. This includes the power to terminate, continue or assign contracts, enter into contracts and service agreements to ensure the continuity of essential services and function; and the purchase and sale of assets. For example, Section 402A of IRMA provides that the rehabilitator may take such action it deems necessary or appropriate to reform and revitalize the insurer, including cancelling policies, insurance and reinsurance contracts, surety bonds or surety undertakings, or transferring policies, insurance and reinsurance contracts, surety bonds or surety undertakings to a solvent assuming insure. The rehabilitator has full power to direct and manage, to hire and discharge employees, and to deal with the property and business of the insurer in resolution. However, in most states, any restructuring of the insurer in a rehabilitation is effected through a rehabilitation plan that is submitted to court (see, for example, Section 13 c of the Life and Health Insurers Rehabilitation and Liquidation Act of New Jersey, and page 448 of the <i>NAIC Receiver’s Handbook for Insurance Company Insolvencies</i> (2009)). Approval will only be granted after appropriate notice to interested parties and, if necessary, a hearing.</p> <p>Findings. Both the DFA and the FDI Act provide the powers required under EC3.3. Under U.S. state insurance receivership laws the commissioner, as described above, may take control and</p> |

⁹⁷ If the contract is transferred, the initial triggering event (e.g., entry into resolution) cannot be invoked to terminate the contract.

⁹⁸ DFA Section 210(a)(1)(B), (D) and (G); (c) and (h).

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| | operate the insurer in resolution in order to achieve its orderly resolution, including restructure or wind down its operation, terminate, continue or assign contracts, enter into contracts and service agreements to ensure the continuity of essential service functions, and purchase or sell assets. However, for many restructuring measures, court approval is required. |
| EC3.4 | The resolution authority has powers to: <p>(i) require that the firm in resolution temporarily provides, to any successor or acquiring entity to which assets and liabilities of the firm have been transferred, services that are necessary to support continuity of essential services and functions related to those assets and liabilities;</p> <p>(ii) require companies in the same group located within the jurisdiction (whether or not they are regulated) to continue to provide services that are necessary to support such continuity to the firm under resolution or to any successor or acquiring entity at a reasonable rate of reimbursement; and</p> <p>(iii) procure necessary services from unaffiliated third parties.</p> |
| Description and findings re EC3.4 | <p>DFA and Banking. Through the aforementioned powers to succeed to all rights and titles, powers and privileges of the firm in resolution under the receivership, the FDIC can continue to provide services to a successor or acquiring entity. Both legislations also afford powers to utilize the services of private persons to assist in carrying out its responsibilities in the management and disposition of assets from the firm under resolution, provided the FDIC determines that such services are the most practicable, efficient and cost effective.⁹⁹ For (ii) the authorities cited the powers to prevent termination of services, governed by contracts, with companies in the same group.¹⁰⁰ Although the FDIC takes over the assets of and operates the covered financial company with all the powers of the members or shareholders, the directors, and the officers of the company, which may allow the FDIC to operate subsidiaries – including non-operational entities - controlled by the covered financial company, the FDIC lacks an explicit statutory power to require companies in the same group, which are not controlled by the firm in resolution, to continue to provide essential services.</p> <p>State Insurance. Since the commissioner as receiver has full power to direct and manage the insurer in resolution, he may choose to continue purchasing services from vendors within or outside of the group that are necessary to continue essential services and functions and continue to provide essential services to any successor or acquiring entity. Fees payable to such vendors as a result of the commissioner’s choosing to continue the service agreements are categorized as administrative expenses generally at the highest rank and fully paid in accordance with the order of distribution even in the case of liquidation (see § 801 of IRMA, § 7434 New York Insurance Law). However, state insurance resolution law does not specifically provide the commissioner with power to force companies, either within or outside of the group, to continue to render services, even temporarily to any successor or acquiring company. It should be noted that section 108 C. of IRMA prohibits the termination of any contract solely on the basis that receivership proceedings have been commenced against the insurer. Previous model laws do not contain a similar prohibition. Where states have adopted section 108 C. of IRMA or a similar provision, the legal framework enables the commissioner to continue to ensure the performance of service contracts to the insurer. This would not appear to be the case for states that have not enacted such a provision. As only six states have adopted IRMA, it is unclear to what degree an IRMA-like framework is in place in the broad majority of states. Moreover, as the IRMA framework does not</p> |

⁹⁹ FDI Act, 12 USC. § 1821(d)(2)(K), and DFA Section 210(a)(1)(L).

¹⁰⁰ FDI Act, 12 USC. § 1821(e)(13)(C)(i), and DFA Section 210(c)(13)(C)(i).

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| | <p>provide for an explicit power to require the continuity of services, it falls short of what is contemplated in EC 3.4.</p> <p>Findings. Both the DFA and the FDI Act lack explicit powers to require companies in the same group (whether or not they are regulated) to continue to provide services, including those not governed by contract, or from firms which are themselves subject to a bankruptcy or resolution proceeding for example, as necessary to support effective resolution. It is recommended that these powers be adopted. A similar approach should be taken with respect to insurance.</p> |
| EC3.5 | <p>The resolution authority has the power to effect the sale of the institution or its merger with another institution, or the transfer of assets or liabilities (including insurance portfolios and holdings of client assets) to a third party, asset management vehicle or bridge institution without requiring prior notification or the consent of any interested private party such as the shareholders, depositors, policyholder or other creditors and clients of the firm in resolution.</p> |
| Description and findings re EC3.5 | <p>DFA and Banking. Both provide the FDIC as receiver with powers to merge the failed institution with another institution and to transfer or sell any asset or liability of the failed institution to a third party (including an asset management vehicle or bridge institutions) without providing prior notification or obtaining approval, assignment or consent with respect to such transfer.¹⁰¹ Ex post notification of the transfer is required by at the latest 5p.m. (eastern time) on the business day following the date of the appointment of the Corporation as receiver, only if financial contracts are transferred.</p> <p>State Insurance. State insurance receivership law typically gives the rehabilitator broad authority to effect the sale of the company in receivership or its merger with another institution, to transfer assets and liabilities (including insurance portfolios) to a third party without the consent of any interested party. However, such powers are invariably exercised through the submission of a rehabilitation plan to a court which will only be approved after notice to interested parties and, if necessary, a hearing. For example, under IRMA, to effect an assumption or reinsurance of all or a portion of the insurer's liabilities by, and transfer of assets and related books and records to, a licensed insurer or other entity, or any other corporate reorganization transaction consistent with the law, the commissioner as receiver is required to prepare and file a plan of rehabilitation with the receivership court within a specified period after entry of the rehabilitation order.</p> <p>The Life and Health Insurers Rehabilitation and Liquidation Act of New Jersey (Section 13) empowers the commissioner as rehabilitator power to effect reorganization, consolidation, conversion, merger or other transformation of the insurer through court approval of an appropriate rehabilitation plan.</p> <p>Findings. Both the DFA and the FDI Act are consistent with EC 3.5. The U.S. state receivership laws generally provide the commissioner as rehabilitator with the power and authority to effect the sale of the insurer in resolution or its merger with another insurer, or transfer of insurance portfolios as well as other assets and liabilities to a third party without requiring prior consent of any interested private party such as the shareholders, policyholders or other creditors and clients of the insurer in resolution. However, prior notice to interested parties and court approval is required for the commissioner to enter into such a corporate reorganization transaction.</p> |
| EC3.6 | <p>The resolution authority has the power to transfer assets or liabilities back from the bridge institution to the firm in resolution, the estate of the firm or to an asset management vehicle. The exercise of that reverse transfer power is subject to appropriate safeguards.</p> |

¹⁰¹ FDI Act, 12 USC. § 1821(d)(2)(G) and (n)(1)(A) and (B), and DFA Sec. 210(a)(1)(G) and (h)(5)(A).

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| Description and findings re EC3.6 | <p>DFA and Banking. The transfer of assets or liabilities from the FDIC receivership to a bridge institution is effected in the U.S. regime through purchase and assumption agreements i.e., a contractual arrangement. Explanatory Note (EN) 3(w) allows for the ability to transfer assets or liabilities back from the bridge institution, and any conditions or safeguards which are applied to be established as a matter of contract. In two sample P&A agreements identified by the authorities¹⁰² a number of assets (e.g., collateral which secures a loan in the receivership) and related liabilities are specified which must be returned by the bridge bank at the request of the FDIC as receiver. The contract specifies the price to be paid by the receiver and the period in which the payment must be made.</p> <p>State Insurance. Under state receivership laws, the commissioner of the state as rehabilitator generally has broad powers and authority to direct and manage, and to deal with the property and business of the insurer in resolution, subject to court approval. However, as discussed in EC3.7, using a bridge institution or an asset management vehicle is not a typical resolution strategy for U.S. domiciled insurers, and is not explicitly envisaged in state resolution frameworks. While state resolution authorities clarified that a rehabilitator could enter into a contract that provided for the retransfer of assets or liabilities back from a bridge institution, the exercise of any such powers by the receiver would be subject to court approval.</p> <p>Findings. Both the DFA and the FDI Act comply with EC 3.5. While it may be possible, at least in some states, for a rehabilitator to enter into a contract providing for the transfer back of assets and liabilities back from a bridge institution, it would require court approval as part of a rehabilitation plan.</p> |
| EC3.7 | <p>The resolution authority has the powers set out in KA 3.4 to establish one or more bridge institutions. The legal framework specifies, or gives the resolution authority the power to specify, the terms and conditions under which a bridge institution will be set up and operate as a going concern, including:</p> <ul style="list-style-type: none"> (i) its ownership structure; (ii) the sources of capital, its operational financing and liquidity support; (iii) the applicable regulatory requirements, including regulatory capital; (iv) the applicable corporate governance framework; and (v) the process for appointing the management of the bridge institution and its responsibilities. |
| Description and findings re EC3.7 | <p>DFA and Banking. The Housing and Economic Recovery Act (2008) extended the bridge powers to all IDIs including thrifts, after the Indymac conservatorship. Under the FDI Act and the DFA the FDIC has the powers to establish one or more bridge institutions,¹⁰³ and to transfer to it assets and liabilities of the failed firm selected by the FDIC. Transfers in practice are effected by legally enforceable agreements.</p> <p>(i) The FDIC has discretion in specifying the other terms and conditions under which a bridge institution will be established and operate as a going concern, including with respect to the bridge institution's ownership structure. Both the FDI Act and the DFA provide that the status of a bridge</p> |

¹⁰² https://www.fdic.gov/bank/individual/failed/ibb_P_and_A.pdf;
https://www.fdic.gov/bank/individual/failed/IndyMac_P_and_A.pdf

¹⁰³ FDI Act, 12 USC. § 1821(n)(1)(A), and DFA Section 210(a)(1)(F) and (h).

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| | <p>institution shall terminate as such upon, among other things, the sale of 80 percent or more of its capital stock to a person or entity other than the FDIC or another bridge institution.¹⁰⁴ Both also set a maximum five years on the life of a bridge.</p> <p>(ii) The FDIC as receiver has the discretion to cause capital stock or other securities of a bridge institution to be issued and offered for sale in amounts and on terms and conditions as the FDIC may determine. In addition, the FDIC has the power to make funds available for the operation of the bridge institution in lieu of capital. The FDI Act also provides that a bridge depository institution will not be deemed undercapitalized for purposes of access to the discount window of the FRB. Under the DFA, the FDIC as receiver may authorize a bridge institution to obtain credit, including on a secured basis. As noted in the SPE strategy notice published by the FDIC,¹⁰⁵ if market conditions mean that private sector funding cannot be immediately obtained, the DFA provides for the OLF to serve as a back-up source of liquidity support, which could be used on a secured basis. The FDIC could also facilitate private-sector funding to the bridge financial company and its subsidiaries by providing guarantees, backed by its authority to obtain funding through the OLF. The DFA does not allow the FDIC to transfer more liabilities than assets to the bridge institution and to cover the shortfall, which could act as a constraint if TLAC was inadequate or it were issued in the wrong place in the group to facilitate effective resolution.¹⁰⁶</p> <p>(iii) Under the FDI Act, the bridge institution will be an insured national bank or federal savings association chartered by the OCC. Under the DFA the FDIC can grant a federal charter and approve the articles of association). The FDIC as receiver is afforded discretion in the manner in which the bridge institution will comply with applicable regulatory requirements. As noted above, with respect to regulatory capital, both the FDI Act and the DFA provide that a bridge institution may operate without any capital or surplus, or such capital or surplus as the FDIC as receiver may in its discretion determine to be appropriate.¹⁰⁷</p> <p>(iv) Under the DFA, a bridge financial company may elect to follow the corporate governance practices and procedures that are applicable to a corporation incorporated under the general corporation law of the State of Delaware, or the state of incorporation or organization of the failed financial company with respect to which the bridge financial company was established. Under the FDI Act, a bridge depository institution may be organized as either a national bank, in the case of one or more insured banks, or as a Federal savings association, in the case of one or more insured savings associations. The FDIC as receiver has broad authority in determining the process for appointing the management of the bridge institution and its responsibilities.</p> <p>(v) Under both the FDI Act and the DFA, the bridge institution is to be under the management of a board of directors whose members are appointed by the FDIC.</p> <p>State Insurance. Under State insurance receivership law, the establishment of a legal entity that functions as a bridge institution, either by the rehabilitator or by another agency or body, and having selected portfolios, assets, liabilities or obligations of the insurer transferred to such legal entity to operate or manage such entity as a going concern has not generally been used to resolve failed insurers and is not explicitly addressed in the legislation. Rather, the commissioner</p> |
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¹⁰⁴ FDI Act, 12 USC. § 1821(n)(10)(C), and DFA Section 210(h)(13)(C).

¹⁰⁵ Resolution of Systemically Important Financial Institutions: The Single Point of Entry Strategy, 78 Federal Register (F.R.) 76614 (December 18, 2013).

¹⁰⁶ DFA Section 210(h)(5)(F).

¹⁰⁷ FDI Act, 12 USC. § 1821(n)(5), and DFA Section 210(h)(2)(G).

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| | <p>as receiver would normally transfer or reinsure the portfolios to a guaranty association to provide for the policy obligations continue to be administered by it (run-off). In some liquidations, special purpose vehicles have been established by the guaranty funds or as a subsidiary of the receivership estate to run off liabilities. While State commissioners expressed the view that the establishment of such an entity would be possible in some states, there is insufficient practice to determine whether such institutions could be established in most states or how the various issues addressed in EC 3.7 would be addressed. In any event, the establishment of such an institution and its operation as a going concern would be subject to court approval.</p> <p>Findings. The FDIC has the powers under both the DFA and the FDI Act to establish one or more bridge institutions as set out in EC 3.7. US state insurance receivership laws do not explicitly provide that a receiver with the powers envisaged in EC 3.7, i.e., to establish one or more bridge institutions to take over viable operations of the failed insurer and continue operating as a going concern. While there is some question as to whether or how the State commissioners or another authority in most states could establish a bridge institution, in the context of a receivership as envisaged under EC 3.7, any such exercise of authority by the commissioner would be subject to court approval in the context of a rehabilitation plan.</p> |
| EC3.8 | <p>The resolution authority has the power, either directly or indirectly, to establish a separate asset management vehicle for the purposes of managing and winding down assets transferred to it from a firm in resolution.</p> |
| Description and findings re EC3.8 | <p>DFA and Banking. The authorities cited the aforementioned powers of the FDIC as receiver to succeed to all rights, titles, powers, and privileges of the entity, take over and transfer its assets and liabilities and operate it with all of the powers of the members or shareholders, directors and officers as enabling it to establish a separate asset management vehicle or equivalent corporate entity and transfer to the vehicle to manage and run-down non-performing loans or difficult-to-value assets.¹⁰⁸ The authorities also cited examples with respect to resolutions of IDIs under the FDI Act, in which the FDIC has used separate asset management vehicles, including securitization vehicles and joint venture equity partnerships, for purposes of transferring non-performing loans or difficult-to-value assets.</p> <p>State Insurance. While stating that the establishment of an asset management vehicle as envisaged under EC 3.8 would be possible with court approval, state authorities clarified that the potential need for an asset management vehicle in an insurance resolution is not great. It is normally the case that almost all of the assets of the insurer will be transferred to a healthy acquirer with the insurance portfolio. As there is little precedent for the establishment of asset management vehicles in the context of state resolution laws, it is unclear to what degree and, under what conditions, such vehicles would or could be used in most states.</p> <p>Findings. The FDIC, in its general capacity as a receiver, has the powers under both FDI Act and the DFA to establish a separate asset management vehicle for the purposes of managing and winding down assets transferred to it from a firm in resolution, as set out in EC 3.8. The US state insurance receivership laws do not explicitly provide for the establishment of an asset management vehicle in a receivership and it is unclear how it would generally be used in a receivership. In any event, the use of an asset management vehicle in the context of a receivership (in particular, the transfer of assets from the failed company) would be subject to court approval.</p> |
| EC3.10 | <p>The resolution authority has the power to give effect to all of the following actions as necessary to absorb losses:</p> |

¹⁰⁸ FDI Act, 12 USC. § 1821(d)(2)(G), and DFA Section 210(a)(1)(G).

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| | <p>(i) cancel or write off equity or other instruments of ownership of the firm;</p> <p>(ii) terminate or write down unsecured and uninsured creditor claims; and</p> <p>(iii) exchange or convert into equity or other instruments of ownership of the firm, any successor in resolution (such as a bridge institution to which part or all of the business of the failed firm is transferred) or the parent company within that jurisdiction, all or parts of unsecured and uninsured creditor claims.</p> |
| <p>Description and findings re EC3.10</p> | <p>DFA. The DFA does not include explicit statutory bail-in powers. The FDIC as receiver has the power to determine claims in accordance with the statutory hierarchy.¹⁰⁹ Through the claims process the FDIC can terminate the claims of equity holders and creditors, and pay them lesser value in accordance with the statutory hierarchy (see EC 5.1), so that such persons bear losses arising from the covered firm’s failure. This approach is consistent with EN 3(x) of the AM. The FDIC can also in effect, exchange equity in a successor to the failed financial company, including a bridge financial company, in satisfaction of claims against the failed financial company in accordance with the statutory hierarchy of claims. The authorities explained that this can be effected through the aforementioned powers to transfer assets and liabilities to a newly established bridge financial company,¹¹⁰ to cause the bridge financial company to issue capital stock or other securities and to convert such liabilities into equity claims in the bridge company or in a new holding company.¹¹¹</p> <p>Consistent with this approach the FDIC is developing a single point of entry strategy (SPE) designed for the resolution of SIFIs potentially subject to Title II.¹¹² Under this strategy, the FDIC would be appointed as receiver to the ultimate U.S. parent holding company of the financial group. Immediately following the FDIC’s appointment as receiver, the FDIC would charter a bridge financial company to which substantially all of the assets of the U.S. parent holding company, including its investments in and loans to subsidiaries (in which the group’s operating assets and liabilities reside) would be transferred. Rights related to equity, subordinated debt and senior unsecured debt of the U.S. parent holding company in resolution would be terminated, except that the right to payment, in resolution or other satisfaction of claims based thereon would be determined pursuant to the claims process of the receivership.¹¹³</p> <p>Under this approach the newly formed bridge financial company would continue to perform the systemically important functions of the failed financial company, thereby minimizing disruptions to the financial system and minimizing the risk of spill-over effects to counterparties. Subsidiaries—both domestic and foreign—of the failed financial company may remain open and operating, with capital and liquidity support where necessary provided by the parent bridge. During this process, the FDIC would undertake measures to address the problems that led to the financial company’s failure. Such measures could include changes to the financial company’s businesses, shrinking those businesses, breaking them into smaller entities, or liquidating certain subsidiaries or business lines or closing certain operations.</p> <p>The SPE strategy envisages providing for the final payment of creditors’ claims through a securities-for-claims exchange six to nine months after establishing the bridge financial company.</p> |

¹⁰⁹ DFA Section 210(b).

¹¹⁰ DFA Section 210(a)(1)(F) and (h).

¹¹¹ DFA Section 210(h)(2)(G)(iii).

¹¹² “Resolution of Systemically Important Financial Institutions: The Single Point of Entry Strategy,” 78 F. R. 76614.

¹¹³ DFA Section 210(a)(1)(M).

Equity in and new debt (including potentially warrants or options) of a new financial company or companies as the successor(s) to the bridge financial company, would be issued to creditors of the failed entity in satisfaction of their claims against the receivership estate of the failed financial company and the bridge would be terminated. While this method of resolving the bridge bank is seemingly not expressly articulated in the FDI Act, and the powers to convert creditors in the receivership into shareholders and creditors of a new company not explicitly covered, the authorities explained that it would be allowed for under the aforementioned process to satisfy creditor claims.

Banking. The FDI Act does not include explicit statutory bail-in powers. In principle, equivalent powers in the FDI Act (as per those in the DFA) could be used to achieve the same economic effect. However, the authorities explained that the no planning has been undertaken, and such an approach has not in practice been needed to be used under the FDI Act.

State Insurance. State insurance receivership law generally authorizes the receiver, subject to certain conditions, to cancel or write off equity or other instruments of ownership of the firm, and to terminate or write down unsecured and uninsured creditor claims. However, it would not appear to explicitly authorize a receiver to exchange claims against the firm into equity in the firm, and it is not clear whether, and under what conditions, a receiver could engage in the type of debt for equity exchange envisaged in a bridge institution operation of the type described in a bank insolvency context described above. Moreover, any such restructuring operations, if possible, could only be effected through court approval after notice and a hearing.

Section 402 of IRMA explicitly empowers a rehabilitator to cancel various obligations of the insurer with court approval (subject to a no creditor worse off principle). Moreover, IRMA (Section 503 (B)) provides that a liquidator may, with court approval, sell the insurer in a way that all outstanding stock of the corporate entity is cancelled, new stock or other securities are authorized and issued to an acquirer (with the acquirer's consent) to effect a change in control of the corporate entity. While these various provisions would suggest that a liquidator could, with court approval, cancel or write off equity, and terminate or write down certain unsecured or insured claims, it is unclear whether such claims could be exchanged on a mandatory basis with equity in the existing or a successor bridge firm. Such operations are, at present, unknown in State insurance receivership law and it is unclear to what degree they would be possible in most states. As a practical matter, it is unclear whether, given the typical liability structure of an insurance company, they would be feasible. In any event, any such operation would be subject to court approval.

Findings. The DFA and the FDI Act include powers which could enable the FDIC to carry out the actions set out in EC 3.10. Specifically, and as allowed for in the KA AM, bail-in could be effected by terminating the corporate rights of shareholders and creditors upon entry into resolution and a claims payment process whereby they bear losses and receive payment for remaining value in the form of equity and debt securities of a newly established company. While retaining flexibility to pursue different strategies depending on the circumstances, it is recommended that authorities afford more clarity e.g., via a final notice or regulation, on a number of key aspects of the approach including on the valuation process and the possible counterfactual of a liquidation under general insolvency laws, the communication strategy to creditors and the legal mechanics for the establishment of the new holding company, the treatment of creditors who would not meet the suitability requirements for shareholders, corporate governance rules applicable to the bridge bank or bridge financial company, the disclosure and registration requirements and related waivers applying in a Title II proceeding, etc. It is not clear to what degree the powers and authority of a state commissioner, in either rehabilitation or liquidation, would permit all of the operations provided for under EC 3.10 under most state insurance resolution regimes. In any event, the implementation of any such strategy could only be implemented with court approval.

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| | Further work on the feasibility of bail-in in the context of an insurance company is warranted. |
| EC3.11 | The legal framework provides clarity as regards the scope of the bail-in power set out in KA 3.5, that is, the range of liabilities covered and provides for its application in a manner that respects the hierarchy of claims as established in KA 5.1. |
| Description and findings re EC3.11 | <p>DFA. Section 206(3) requires the FDIC in all OLA actions to ensure that unsecured creditors bear losses in accordance with the hierarchy of claims in Section (see EC 5.1).</p> <p>Although section 215 of the DFA commissioned the FSOC to study haircuts on secured creditors¹¹⁴ Title II protects fully secured creditors, only allowing for any under-collateralized portion of a secured claim to be treated accordance with the hierarchy above.¹¹⁵ As provided for under KA 5.1 the DFA gives the FDIC discretion to treat pari passu creditors differently under a limited set of circumstances (see EC 5.2). The FDIC has stated that it would not exercise its discretion in this regard in a manner that would result in preferential treatment to holders of long-term senior debt (defined as unsecured debt with a term of longer than one year), subordinated debt, or equity.¹¹⁶ The authorities explained that in most cases, general creditor claims such as long-term unsecured debt would be subject potentially to conversion to equity in a bridge financial company or successor entity. Such debt would not be limited to pre-defined instruments such as contingent capital. Further clarity however on the likely treatment of different types of creditors of the same class e.g., operational liabilities versus long-term bonds, is expected to come from the refinement of resolution plans, and group structures to enhance resolvability, including finalizing and implementing the TLAC rule.</p> <p>Banking. If in a resolution of an IDI the FDI Act powers were used to achieve the economic effect of bail-in, the creditor hierarchy would need to be followed, subject to exceptions set forth below (see ECs 5.1 and 5.2).</p> <p>State Insurance. As described in EC 5.1, State resolution regimes set out a hierarchy of claims that must be respected in a liquidation and, in rehabilitation. Any cancellation or write down of claims against the company would need to respect the hierarchy of claims. However, as noted above, it is not clear to what degree the operations contemplated in EC 3.11 would be possible under most state insurance resolution regimes.</p> <p>Findings. While the DFA and the FDI Act meet the requirements in EC 3.11, more clarity over the relative treatment of unsecured creditors in the same class, while preserving necessary flexibility to effect an OLA resolution of a complex SIFI, would improve predictability for creditors. The FDIC should issue more guidance and information once the TLAC proposals are finalized. As observed in EC 3.10, it is not clear to what degree most state insurance resolution regimes would permit the full range of bail in powers.</p> |
| EC3.12 | <p>The legal framework enables the resolution authority to require or bring about, including through application to the court or through another authority, all of the following actions where necessary to give effect to the write-down or conversion, quickly and without the need for existing shareholder consent:</p> <p>(i) the cancellation of share capital and instruments;</p> |

¹¹⁴ <http://www.treasury.gov/initiatives/Documents/Report%20to%20Congress%20on%20Secured%20Creditor%20Haircuts.pdf>

¹¹⁵ DFA 210(a)(3)(D), and (b)(5).

¹¹⁶ See 12 C.F.R. § 380.27.

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| | <p>(ii) the issuance of new shares or other instruments of ownership;</p> <p>(iii) the overriding of pre-emption rights of existing shareholders of the firm;</p> <p>(iv) the issuance of warrants to equity holders or subordinated (and if appropriate senior) debt holders whose claims have been subject to bail-in (to enable adjustment of the distribution of shares based on a further valuation at a later stage); and</p> <p>(v) the suspension of shares and other relevant securities from listing and trading for a temporary period.</p> |
| Description and findings re EC3.12 | <p>DFA and Banking. As noted above the FDIC as receiver succeeds to all rights, titles, powers, and privileges of the institution as well as its shareholders or members, and may take over the assets of and operate the entity with all of the powers of the members or shareholders, directors and officers and conduct all business of the entity. This authority enables the FDIC as the resolution authority to cancel existing share capital and instruments; issue new shares or other instruments of ownership, including warrants; and override pre-emption rights of existing shareholders.¹¹⁷ The framework does not provide powers for the temporary suspension of shares and other relevant securities from listing and trading, as all the DFA and FDI Act receivership powers are exercised on a closed-firm basis. Accordingly, the institution will, as a matter of course, be de-listed from any exchanges on which its shares formerly traded.</p> <p>State Insurance. IRMA explicitly provides that upon the application by the commissioner as liquidator to sell the corporate entity or charter, the receivership court may cancel all outstanding stock and other securities of, or other equity interests in, the corporate entity or charter, provided that the cancellation shall not affect any claim against the estate by holders of the equity interests (Section 503 B (2)). To the extent that the institution is placed into liquidation, it would, as a matter of course, be de-listed from any exchanges on which its shares formerly traded.</p> <p>Findings. With the exception of (v) which may not be pertinent to the US approach (but not explicitly exempted under the KA AM and is discussed under EC 5.7) the authorities have the powers set out in EC 3.12 with respect to banking. U.S. state insurance receivership laws generally provide the commissioner as liquidator with powers and authority to sell or dissolve the corporate entity or charter of an insurer in resolution separate from the claims of its creditors and interests of its stockholders under court supervision. As noted above, it is not clear to what degree these powers could be exercised in a manner that could effect a bail-in of debt as contemplated in EC 3.10. In any event, any such operations would be subject to court approval.</p> |
| EC3.13 | <p>The legal framework enables contingent convertible instruments not triggered prior to entry into resolution to be terminated, written down or converted in accordance with the particular contractual terms immediately on entry into resolution, and enables bail-in powers to be applied to those instruments, or claims resulting from their termination, contractual write-down or conversion, pari passu with instruments of the same type, except if necessary to contain the potential systemic impact of a firm's failure or to maximise the value for the benefit of all creditors as a whole (see KA 5.1).</p> |
| Description and findings re EC3.13 | <p>DFA and Banking. The legal framework in the U.S. does not differentiate between contingent convertible instruments not triggered prior to entry into resolution and other types of unsecured debt. Accordingly, contingent convertible instruments not triggered prior to entry into resolution may be terminated and allocated losses through the claims process in accordance with the particular contractual terms immediately on entry into resolution. The economic effect of these</p> |

¹¹⁷ FDI Act, 12 USC. § 1821(d)(2) and (n)(5)(C), and DFA Section 210(a)(1)(A), (a)(1)(M) and (h)(2)(G)(iii).

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| | <p>powers would be to treat the instruments or claims <i>pari passu</i> with claims of creditors of the same class, subject to the exceptions set forth below.¹¹⁸ As discussed in greater detail in EC 5.2, the FDI Act and the DFA allow the FDIC to depart from the principle of equal treatment of creditors. The FDIC has stated however that it would not exercise its discretion under the DFA to treat similarly situated creditors differently in a manner that would result in preferential treatment to holders of long-term senior debt (defined as unsecured debt with a term of longer than one year), subordinated debt (included contingent convertible, or equity).¹¹⁹</p> <p>State Insurance. Under the broad powers and authority given to commissioner as receiver, the commissioner may, upon court approval, value claims and assign losses to creditors by, for example, terminating corporate rights, writing down unsecured creditor claims in a way consistent with the hierarchy of creditors and <i>pari passu</i> with instruments of the same type. Neither IRMA nor state insurance resolution laws makes reference to unsecured debts with contingent feature and the issuance of contingent convertible instruments by an insurance company would appear to be rare. It is, therefore, difficult to envisage how the operations envisaged in EC 3.13 would operate in the context of a state insurance receivership.</p> <p>Findings. Contingent convertible instruments not triggered prior to entry into resolution can be terminated, written down or converted under the DFA and DFIA. It would appear that contingent convertible instruments if issued by an insurance company could be terminated or written down in receivership with court approval.</p> |
| EC3.15 | A resolution authority that is responsible for the resolution of insurers has the power to restructure, limit or write down insurance and reinsurance liabilities and allocate losses to creditors and policyholders in a way consistent with the statutory creditor hierarchy. |
| Description and findings re EC3.15 | State Insurance. State insurance resolution regimes generally authorize the receiver, subject to certain conditions, to restructure, limit or write-down liabilities (including insurance and reinsurance liabilities) and allocate losses to creditors in a way consistent with the statutory creditor hierarchy. Any such restructuring would be subject to court approval—for example, as part of a rehabilitation plan. In practice, policyholders, categorized as superior creditors (class 3), generally receive payment of claims from estate assets in the normal course; i.e., the plan does not specify insurance liabilities as being subject to moratorium, and, with a support of the guaranty fund in case of liquidation, the life and annuity business is normally sold to a healthy insurer. In liquidation, property and casualty insurance may be cancelled after the lapse of a statutory period (Section 502B of IRMA) and the liabilities owed by the insurer will be subject to limitation or write-down in a way consistent with the statutory creditor hierarchy. If the insurer in resolution assumes reinsurance from other insurer, then the reinsurance liabilities are not reduced as a result of the resolution proceeding (Section 611A of IRMA). |
| EC3.16 | The resolution authority has the power to impose a moratorium (stay of creditor actions to attach assets or otherwise collect money or property from the firm and suspension of payments). |
| Description and findings | DFA and Banking. Both legislations impose a statutory stay on the exercise of creditor actions to attach assets or otherwise collect money or property from the firm. ¹²⁰ For contracts other than |

¹¹⁸ FDI Act, 12 USC. § 1821(d)(11), and DFA Section 210(b)(1).

¹¹⁹ See 12 C.F.R. § 380.27.

¹²⁰ For details on the temporary stay which applies to qualified financial contracts see EC 4.2.

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| re EC3.16 | <p>financial contracts (see KA 4), there is generally a 90-day stay in which the parties cannot terminate the contract or obtain control of the institution's property.¹²¹ With respect to payments and property transfers to central counterparties and financial contracts entered into the payment, clearing and settlements systems, under the DFA, if the FDIC as receiver fails to satisfy margin, collateral or settlement obligations (other than those that are unenforceable under the DFA) that arise under a financial contract cleared by or subject to the rules of the clearing organization as required by the rules of the clearing organization, the clearing organization has the right to exercise its default remedies.¹²² In addition, the legal framework provides that no property of the FDIC shall be subject to levy, attachment, garnishment, foreclosure, or sale without the consent of the FDIC, nor shall any involuntary lien attach to the property of the FDIC.¹²³</p> <p>State Insurance. The commencement of a receivership proceeding under U.S. state resolution law generally operates as a stay, applicable to all persons on the commencement or continuation of judicial, administrative or other action or proceeding against the insurer, including arbitration proceedings, that was or could have been commenced before the commencement of the delinquency proceeding, or to recover a claim against the insurer that arose before the commencement of the delinquency proceeding.¹²⁴</p> <p>For example, under N.J.S.A 17B--53 of the Life and Health Insurers Rehabilitation and Liquidation Act of New Jersey, upon issuance of an order appointing a liquidator, no action at law or equity or in arbitration shall be brought against the insurer or liquidator, nor shall any existing actions be maintained or further presented after issuance of that order. Although state practice differs to some degree the courts of other states will give full faith and credit to injunctions obtained by the liquidator or the continuation of existing actions against the liquidator or the insurer, when those injunctions are included in an order to liquidate an insurer issued pursuant to corresponding provisions in other states.</p> <p>Findings. The resolution authority has the power to impose a moratorium (stay of creditor actions to attach assets or otherwise collect money or property from the firm and suspension of payments).</p> |
| EC3.17 | <p>In the resolution of an insurer, the resolution authority has the power to temporarily restrict or suspend the rights of policy holders to withdraw from their insurance contracts which may be exercised in a way appropriate to the nature of the insurance contract.</p> |
| Description and findings re EC3.17 | <p>State Insurance. The commissioner as the resolution authority has the power, with court approval, to temporarily restrict or suspend the rights of policyholders to withdraw from their insurance contracts. Under New York Insurance Law, the superintendent as receiver has broad power and authority to deal with property and business of the insurer in resolution in accordance with the court order.¹²⁵ As such, the superintendent as receiver may, under the court order, restrict or suspend the rights of policyholders for a period of time, such as to suspend claim payments and halt the transfer of cash or loan values on life insurance contracts.</p> <p>Findings. Under the U.S. state insurance resolution law, the receiver, with court approval, has the power to temporarily restrict or suspend the rights of policy holders to withdraw from</p> |

¹²¹ FDI Act, 12 U.S.C. § 1821(e)(13)(C)(i), and DFA Section 210(c)(13)(C)(i).

¹²² DFA Section 210(c)(8)(G).

¹²³ FDI Act, 12 U.S.C. § 1825(b)(2), and DFA Section 210(q)(1)(B).

¹²⁴ IRMA Section 108.

¹²⁵ New York Insurance Law Section 7405 (a) in the case of liquidation.

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| | their insurance contracts. |
| EC3.18 | <p>The resolution authority has the power to effect the closure and orderly wind-down and liquidation of the whole or part of a failing firm, and in such event, has the capacity and practical ability to effect or secure any of the following:</p> <p>(i) the timely pay-out to insured depositors, insurance policy holders or other protected clients;</p> <p>(ii) the prompt transfer of insured deposits or insurance contracts to a third party or bridge institution;</p> <p>(iii) the timely transfer or return of client assets.</p> |
| Description and findings re EC3.18 | <p>DFA and Banking. The FDIC as the resolution authority has broad powers to effect the closure and orderly wind-down and liquidation of the whole or part of a failing institution and has a long track of liquidating IDIs.¹²⁶ With respect to insured deposits, these powers provide the FDIC with the capacity and practical ability to pay claims on account of such deposits as soon as possible either in cash from the Deposit Insurance Fund or by making available to each depositor a transferred deposit in a new IDI.¹²⁷ To the extent an IDI holds non-deposit client assets in a trust or similar fiduciary capacity, such assets are treated separately from the other assets of the failed IDI and would be returned to the client or transferred to a bridge bank or a new IDI.</p> <p>State Insurance. Under state insurance receivership law, the commissioner upon the granting of a liquidation order will be vested with broad powers to effect the closure and orderly wind-down and liquidation of the whole or part of the insurer, subject to court approval. Upon issuance of the order of liquidation, the rights and liabilities of the insurer and of its creditors, policyholders, shareholders and all other persons interested in its estate become fixed as of the date of entry of the order. The rights of creditors—including policyholders—are paid out in accordance with order of hierarchy of creditors.</p> <p>For example, under Section 7405 of the New York Insurance Law, upon issuance of a liquidation order, the rights and liabilities of the policyholders are, unless otherwise directed by the court, fixed as of the date of order and, if the claim is proved under Section 7433 (a), then the distribution will be made in accordance with the priority set forth in Section 7434 (a). Due to the broad powers and authority given by the superintendent as liquidator under Section 7409 (b), the superintendent may, in accordance with the court order, transfer insurance contracts to a third party or engage in commutation, thereby timely return of (a part of) the value of contract is accomplished.</p> <p>Findings. The resolution authority has the power to effect the closure and orderly wind-down and liquidation of the whole or part of a failing firm including the timely pay-out or transfer of insured deposits, and prompt transfer or return of client assets and transfer of insurance contracts. In the case of state insurance resolution, the exercise of these powers is subject to court approval, with notice to affected parties and a hearing.</p> |
| EC3.19 | In the resolution of an insurer the resolution regime enables the writing of new business to be discontinued once the firm is placed in resolution while existing contractual policy obligations continue to be administered (run-off). |
| Description and findings | State Insurance. Under state insurance receivership regimes, run-off is possible through administrative supervision (solvent run-off) or in a rehabilitation or liquidation proceeding |

¹²⁶ FDI Act, 12 USC. § 1821(d), and DFA Section 210.

¹²⁷ FDI Act, 12 USC. § 1821(f).

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| re EC3.19 | <p>(insolvent run-off).</p> <p>In practice, how to deal with run-off differs among the property and casualty insurers and life and health insurers. In case of property and casualty insurers, new policies may be discontinued and the claims may be handled in a run-off through administrative supervision or in a rehabilitation proceeding. In a liquidation proceeding, existing policies must be cancelled; claims on cancelled policies are transferred to a guarantee association or classified as claims in the receivership, as applicable.</p> <p>In case of life and health insurers, new policies may be discontinued and the claims may be handled in a run-off in a rehabilitation proceeding. For insurers in liquidation, guaranty associations are required to take measures to assure payment of the insurer's policyholder obligations. In most life insurance insolvencies, the guaranty associations will act to facilitate the transfer of policies and contracts to a financially stable insurer, or will otherwise provide a financial support for the run-off of the insurer's policies and contracts and will receive distributions from the estate to the extent possible in repayment of those Guaranty Association expenditures.</p> |
| EC3.20 | The legal framework does not restrict the resolution authority from combining resolution actions and does not require it to apply such actions in a particular order. |
| Description and findings re EC3.20 | <p>DFA and Banking. As noted above, the FDIC has broad authority to manage the resolution of a failed institution.¹²⁸ This broad authority includes the power to combine resolution actions and the discretion to apply such actions in the order the FDIC as receiver determines to be most appropriate to achieve the objectives of resolution.</p> <p>State Insurance. Under state insurance receivership regimes, a receiver has broad authority to choose the appropriate combination of available powers to be included in a rehabilitation or liquidation plan to be submitted to a court. However, any such use will be subject to approval by the receivership court after notice to interested parties and a hearing.</p> <p>Findings. The legal framework does not restrict the resolution authority from exercising its resolution powers separately or in any combination and does not require the resolution authority to take any such actions in a particular order.</p> |
| Assessment of KA3 | |
| Comments | <p>The resolution regime under the DFA and for banks under the FDI Act is closely aligned with KA3. However, clarity should be afforded to the triggers that apply under the DFA, in particular to make clear they apply suitably early at a point of non-viability. In addition the authorities should adopt powers in both the DFA and the FDI Act that would allow the FDIC to require companies in the same group (whether or not they are regulated) to continue to provide services, including those not governed by contract, or party with an entity in bankruptcy, for example, as necessary to support effective resolution. Finally it is recommended, although not required in the AM, that the FDIC issue a final notice or regulation, clarifying in further details key aspects of the SPE approach including with regard to the valuation process, the communication strategy, and the legal mechanics for establishing a new holding company, the treatment of creditors who would not meet the suitability requirements for shareholders, the disclosure and registration requirements and related waivers applying in a Title II proceeding.</p> <p>Some powers contemplated under KA 3 are quickly and readily available to receivers under state receivership laws (e.g., taking control, stays and moratoria) while, others (i.e., most restructuring powers) are only available in the context of a court-approved rehabilitation or liquidation plan,</p> |

¹²⁸ FDI Act, 12 U.S.C. § 1821(d), and DFA Section 210.

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| | <p>with notice to affected parties and, if necessary a hearing. This process is designed primarily to ensure policy holder protection rather than to meet the wider objectives of financial stability. The role of the court in the state receivership process raises two fundamental issues respecting the availability of the resolution powers contemplated in KA 3. First, with respect to those powers that are unknown in state insurance receivership proceedings (e.g., bail in), it is not possible, in the absence of precedent, to conclude that these powers would be readily available to receivers. More generally, a fundamental problem with availability of most restructuring powers is the time that may be necessary to obtain court approval. The US court system is highly efficient and judges generally extend a high level of deference to state insurance commissioners in a resolution but, the potential for delays in obtaining approval may not, in all cases, be fully consistent with the requirements of timeliness envisaged in the Key Attributes. The KA and the AM acknowledge that “it is not necessarily inconsistent with the KA if the resolution regime makes provision for a court order or confirmation for the exercise of resolution powers to be effective” but note that “it is important to ensure that any requirement for court approval does not impede rapid intervention and the ability to achieve the objectives of resolution.” In providing guidance as to the appropriate standard of speed, EN 5 (e) notes that timely exercise of resolution powers “could be facilitated by a legal framework that provides” for, inter alia, (i) “expedited procedures (for example, with shortened notice, filing and decision deadlines for appeals)”; and “applications by the resolution authority without notice to the firm or other affected parties”. Generally, it would not appear that a U.S. insurance resolution authority could obtain court approval for the exercise of the full range of resolution powers with the necessary speed contemplated by this standard. While the KA recognize that the timelines needed for more traditional insurance resolution techniques (e.g., timely pay out of policy holders or for run off) may take longer than envisaged in a bank resolution context, the KA do not otherwise differentiate between the timelines needed for banks and insurers.</p> |
| <p>4. Set-off, Netting, Collateralisation, Segregation of Client Assets</p> | |
| <p>KA4.1</p> | <p>The legal framework governing set-off rights, contractual netting and collateralisation agreements and the segregation of client assets should be clear, transparent and enforceable during a crisis or resolution of firms, and should not hamper the effective implementation of resolution measures.</p> |
| <p>KA4.2</p> | <p>Subject to adequate safeguards, entry into resolution and the exercise of any resolution powers should not trigger statutory or contractual set-off rights, or constitute an event that entitles any counterparty of the firm in resolution to exercise contractual acceleration or early termination rights provided the substantive obligations under the contract continue to be performed.</p> |
| <p>KA4.3</p> | <p>Should contractual acceleration or early termination rights nevertheless be exercisable, the resolution authority should have the power to stay temporarily such rights where they arise by reason only of entry into resolution or in connection with the exercise of any resolution powers. The stay should:</p> <ul style="list-style-type: none"> (i) be strictly limited in time (for example, for a period not exceeding 2 business days); (ii) be subject to adequate safeguards that protect the integrity of financial contracts and provide certainty to counterparties (see Annex IV on Conditions for a temporary stay); and (iii) not affect the exercise of early termination rights of a counterparty against the firm being resolved in the case of any event of default not related to entry into resolution or the exercise of the relevant resolution power occurring before, during or after the period of the stay (for example, failure to make a payment, deliver or return collateral on a due date). <p>The stay may be discretionary (imposed by the resolution authority) or automatic in its operation. In either case, jurisdictions should ensure that there is clarity as to the beginning and the end of the stay.</p> |
| <p>KA4.4</p> | <p>Resolution authorities should apply the temporary stay on early termination rights in accordance with</p> |

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| the guidance set out in Annex IV to ensure that it does not compromise the safe and orderly operations of regulated exchanges and FMIs. | |
| Essential criteria | |
| EC4.1 | The legal framework requires firms to maintain effective arrangements for the identification and safeguarding of client assets that facilitate rapid identification of which assets are client assets and support legal clarity about the nature of the claims and entitlements of individual clients to those assets and clear rules as to how losses are shared between clients in the event of shortfalls in a pool of client assets. |
| Description and findings re EC4.1 | <p>DFA. Different statutes provide for requirements to separately account for client assets in the books and records of regulated financial entities (e.g., futures commission merchants, collective investment schemes), and to segregate client assets from such entities' own funds and from funds of other persons.</p> <p>Banking. Banks authorized by the OCC to hold assets in a fiduciary capacity shall segregate such assets from the general assets of the bank. In the event of failure of the bank, the owners of the funds held in trust for investment shall have a lien on the bonds or other securities so set apart.¹²⁹</p> <p>IDI's may hold client assets as a depository of a financial intermediary. For instance, client assets deposited by a futures commission merchant with a bank must be held under an account identifying the funds as belonging to the clients of the futures commission merchant and held in segregation according to the Commodity Exchange Act. Future commission merchants are required to obtain a letter from the IDI acknowledging that the funds deposited represent client assets under the Commodity Exchange Act and that the IDI may not offset any obligation that the depositing future commission merchant may have with the IDI as a depository by the funds maintained in a segregated account. Likewise, IDIs are eligible custodians of collective investment schemes, which must place their securities and similar investments in the custody of selected custodians. Brokers and dealers must maintain a special reserve account separate from their other bank accounts,¹³⁰ and enter into a written agreement with the bank that the funds in such reserve account shall not be used directly or indirectly as security for a loan and must maintain a "no-lien letter" from the bank acknowledging this limitation.¹³¹</p> <p>The FDI Act provides for a general claims process according to which the FDIC determines whether to allow or disallow claims against an IDI filed with the FDIC as receiver. The FDIC as a receiver may disallow any portion of a claim or claim of security, preference or priority which is not proved to its satisfaction.¹³² The rules applicable on loss sharing between clients in the event of shortfall in the pool of client assets are subject to different laws, depending on which entity is being subject to an insolvency or liquidation proceeding. For instance, in case of liquidation of a futures commission merchant, the trustee shall distribute "customer property" to clients of futures commission merchants, in priority to all other claims with the exception of claims attributed to the administration of such property. Any shortfall is mutualized <i>pro rata</i>, on the basis of allowed net equity claims, among clients of the futures commission merchant.¹³³</p> |

¹²⁹ 12 U.S.C. § 92^a.

¹³⁰ 17 C.F.R. 240.15c3-3(e).

¹³¹ 17 C.F.R. 240.15c3-3(f).

¹³² FDI Act, 12 U.S.C. § 1821(d)(5) and (6).

¹³³ See Section 761(10) and 766(h) of the Bankruptcy Code and 17 CRF §190.08

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| | <p>State Insurance. No specific issues arise in this context.</p> <p>Findings. The U.S. legal framework requires firms to maintain effective arrangements for the identification and safeguarding of client assets.</p> |
| EC4.2 | <p>The legal framework does not establish or contain any statutory or common law set-off rights that arise solely by virtue of either a firm’s entry into resolution or the exercise of resolution powers against that firm and prohibits the exercise by counterparties of early termination rights that arise by reason only of the entry into resolution or the exercise of any resolution power against that firm, except as provided in EC 4.3.</p> |
| Description and findings re EC4.2 | <p>DFA. Counterparties to QFCs with a covered financial company may not exercise any right that such counterparty has to terminate, liquidate or net such contract solely by reason of, or incidental to, the appointment of the FDIC as a receiver for the covered financial company (or the insolvency or financial condition of the covered financial company) for a certain period of time (See also description and findings for EC4.3).¹³⁴</p> <p>In relation to other types of contracts, subject to limited exceptions, counterparties to such contracts with a covered financial company are prohibited from exercising any right to terminate, accelerate or declare a default under such contracts or to obtain possession or exercise control over any property of the failed financial institution or affect any contractual rights of the covered financial company without the consent of the FDIC as receiver during the 90-day period commencing on the date of appointment of the FDIC as receiver.¹³⁵ These contracts are enforceable by the FDIC as receiver notwithstanding any contractual term providing for the termination, default, acceleration or exercise of rights upon, or solely by reason of, insolvency or the appointment of the FDIC as a receiver, the filing for the petition for the commencement of an orderly liquidation, the issuance of a recommendation in connection thereto, or the exercise of powers or rights by the FDIC.¹³⁶ Therefore, while set-off rights may be exercised, above limitations on early termination rights would apply.</p> <p>Banking. The FDI Act contains provisions analogous to those noted above, with respect to the (i) non enforceability of QFCs for a limited period of time,¹³⁷ (ii) the prohibition for non-QFC counterparties of IDIs under resolution to exercise any right of termination, default or acceleration to obtain possession of or exercise control over any property of the IDI or affect any contractual rights of the IDI without the FDIC’s consent for a period of 90 days¹³⁸ and (iii) the power of the FDIC to enforce contracts notwithstanding any provision providing for termination, default, acceleration or exercise of rights solely as a reason of the commencement of a resolution proceeding.¹³⁹</p> <p>State Insurance. In the U.S., there are statutory or common law set-off rights that arise solely by virtue of the insurer’s entry into resolution or exercise of resolution powers against the insurer. However, under some state receivership laws, the commencement of a receivership proceeding operates as a stay on the termination of contracts if the sole basis thereof is an entry into</p> |

¹³⁴ DFA Section 210(c)(10).

¹³⁵ DFA Section 210(c)(13)(C)(i).

¹³⁶ DFA Section 210(c)(13)(A).

¹³⁷ FDI Act, 12 U.S.C. § 1821(e)(10)(B).

¹³⁸ FDI Act, 12 U.S.C. § 1821(e)(13)(C).

¹³⁹ FDI Act, 12 U.S.C. § 1821(e)(13)(A)..

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| | <p>resolution or in connection with the exercise of any resolution power against the insurer.</p> <p>For example, Section 108 C(8) of IRMA provides that the commencement of a delinquency proceeding operates as a stay on the termination, suspension of performance, declaration of default or other adverse action with respect to any contract solely, applicable to all persons, to the termination, suspension of performance, declaration of default or other adverse action with respect to any contract (including without limitation policies and insurance contracts), whether or not the insurer is a party to the contract, if the sole basis therefore is the fact that the insurer is the subject of delinquency proceedings and/or the fact that one or more of the insurer's licenses have been suspended or revoked because the insurer is the subject of delinquency proceedings. In cases where the provision of IRMA are not fully reflected in state receivership law, it is generally open to the receiver, in the context of a delinquency proceeding, to specifically request a stay order upon application for the receivership with the receivership court.</p> <p>However, as discussed in greater detail below, many states (currently 21) have incorporated a "safe harbor" into their receivership legislation (as provided for in Section 711 of IRMA and model provisions developed by the NAIC) to exclude QFCs from the scope of any stay imposed in connection with the commencement of receivership proceedings. The effect of this framework is to permit early termination and netting of QFCs solely as a result of the commencement of receivership proceedings or the exercise of resolution powers in the context of such proceedings.¹⁴⁰</p> <p>Findings. The U.S. regime precludes, in connection with both the DFA and the FDI Act, the exercise by counterparties of firms under resolution of early termination rights that arise solely by reasons only of the entry into resolution of such firm or the exercise of resolution powers. Likewise, counterparties to QFCs cannot exercise set-off rights, for reasons that are based solely on the above mentioned grounds and in connection with a limited period of time. Counterparties of contracts other than financial contracts can exercise early termination rights 90 days after the appointment of the FDIC as a receiver. While set-off rights may be exercised in relation to such contracts, the above limitations on the exercise of early termination rights would apply.</p> <p>With respect to some state insurance resolution regimes, entry into resolution may not permit early termination or set off rights, as the commencement of a proceeding may operate as a stay on the termination of contracts. In many states, however, this is not the case with QFCs.</p> |
| EC4.3 | <p>Where certain contracts or arrangements (for example, financial contracts) are not subject to the prohibition referred to in EC 4.2, the legal framework provides, in relation to such contracts, for a temporary stay on the exercise of early termination rights that arise by reason only of entry into resolution or in connection with the exercise of any resolution powers, subject to the conditions set out in points (i) to (iii) of KA 4.3 and section 2 of Annex IV to the Key Attributes. Those conditions include, in particular, that:</p> <p>(i) where the contracts to which the early termination right relates are transferred to another entity or remain with a firm that has been recapitalised in resolution, early termination rights can be exercised after the expiry of the stay period only in the event of a separate default under the terms of the contract that is not based on the entry into resolution or the exercise of resolution powers;</p> <p>(ii) where those contracts remain with the failing firm that has not been recapitalised, any early termination rights that were subject to the stay may be exercised immediately on the expiry of the stay or, if earlier, a notification by the resolution authority that the contracts will remain with that</p> |

¹⁴⁰ IRMA Section 108 E (4) and (8).

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| | failing firm. |
| Description and findings re EC4.3 | <p>DFA. Early termination rights against a covered financial company arising by reason only of the entry into resolution or the exercise of any resolution power against such company are subject to a temporary stay.¹⁴¹</p> <p>In particular, as regards QFCs, counterparties of the covered financial company cannot exercise any right to terminate, liquidate or net such contract solely by reason of, or incidental to, the appointment of the FDIC as a receiver or due to the financial condition or insolvency of such company (i) until 5:00 p.m. (Eastern Time) on the business day following the date of the appointment or (ii) after the person has received notice that the contract has been transferred.¹⁴² This temporary stay remains in effect with respect to each QFC for the full period described above, even if the FDIC as receiver informs the counterparty prior to the end of such period that the QFCs between the counterparty and the failed financial institution will not be transferred. Such notice, however, is not given in practice: if the contracts are not transferred, early termination rights can be exercised upon the expiration of the stay. If the contracts are transferred, early termination rights can be exercised after the transfer only in the event of a separate default under the terms of the contract that is not based on the entry into resolution, the financial condition or insolvency of the covered financial company, or the exercise of resolution powers.</p> <p>In the case the FDIC has been appointed receiver for a covered financial company that is party to a QFC cleared by or subject to the rules of a clearing organization, if the FDIC as receiver fails to satisfy any margin, collateral or settlement obligation as required by the rules of the clearing organization when due, the clearing organization—without prejudice to the above mentioned temporary stay—has the immediate right to exercise its rights and remedies under its rules with respect to the QFC, including the right to liquidate all positions and collateral under such contracts.¹⁴³</p> <p>The FDIC as receiver for a covered financial company (or for a subsidiary of a covered financial company) shall have the power to enforce contracts of subsidiaries or affiliates of the covered financial company, the obligations under which are guaranteed or supported by, or linked to, the covered financial company, notwithstanding contractual provisions that give rise to termination, liquidation or acceleration rights based on the financial condition, insolvency or receivership of the covered financial company, if (i) such guaranty or other support and all related assets and liabilities are transferred to and assumed by a bridge financial company or a third party (other than a third party subject to a bankruptcy or insolvency proceeding) within the same period of time as the FDIC is entitled to transfer the QFCs of such covered financial company; or (ii) the FDIC, as receiver, otherwise provides adequate protection with respect to such obligations and gives notice thereof within the same time limit as (i) above.¹⁴⁴</p> <p>Banking. The FDI Act contains provisions analogous to those noted above in connection with the</p> |

¹⁴¹ DFA Section 210 (c) (10) (B) and 13 (C). It should be noted that in November 2014, 18 major institutions have agreed to enter into a new ISDA Resolution Stay Protocol, in accordance to which the adhering parties shall opt in to the statutory stay provisions in the special resolution regime of six jurisdictions (including the U.S., with respect to the regime under both DFA Title II and the FDI Act).

¹⁴² DFA Section 210(c)(10)(B).

¹⁴³ DFA Section 210(c)(8)(G).

¹⁴⁴ DFA Section 210(c)(16). *See also* 12 C.F.R. § 380.12.

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| | <p>temporary stay. However, the specific power to enforce contracts of subsidiaries or affiliates, described above, is not included in the FDI Act.¹⁴⁵</p> <p>State Insurance. U.S. state receivership laws do not generally provide for the framework envisaged under EC 4.3 under which the resolution authority may impose a temporary stay on the early termination of financial contracts to facilitate the transfer of those contracts to a healthy institution.</p> <p>As noted above, 21 states have put in place (in some cases with modifications) provisions establishing a “safe harbor” for QFCs that is designed to exclude such contracts from the scope of any stay on early termination and close out arising by virtue of the commencement of receivership proceedings.</p> <p>While the NAIC has issued a “Guideline for Stay on Termination of Netting Agreements and Qualified Financial Contracts” under which a counterparty to a netting agreement or QFC with an insurer in resolution may not exercise the right to terminate, liquidate, accelerate or close out the obligations with respect to the contract by reason of the financial condition of the insurer or by the commencement of a delinquency proceeding until 5:00 p.m. (eastern time) on the business day following the date of appointment of a receiver, or after such counterparty has received notice that the contract has been transferred, the guideline, at this stage, has been enacted into law to a very limited extent.</p> <p>Findings. Qualified financial contracts and other types of contracts are subject to a temporary stay, according to both the DFA and the FDI Act, prohibiting the exercise of early termination rights within a certain period. The FDI Act lacks a mechanism envisaged under the DFA, vesting the FDIC with the power to enforce contracts of subsidiaries or affiliates of the covered financial company for which the FDIC acts as a receiver, notwithstanding the existence of early termination rights based solely on the entry into resolution or the exercise of resolution powers.</p> <p>U.S. state receivership laws do not generally provide for a temporary stay on the early termination of financial contracts.</p> |
| EC4.4 | <p>Under the legal framework, any contract with a domestically incorporated financial institution that contains early termination rights is subject to either a prohibition in accordance with EC 4.2 or a temporary stay in accordance with EC 4.3. Where the legal framework includes both kinds of provision, it is clear in advance, for any type of such contract, which provision would apply to those early termination rights in a resolution of the financial institution under the domestic regime.</p> |
| Description and findings re EC4.4 | <p>DFA and Banking. The U.S. legal framework includes both a prohibition in accordance with EC 4.2 to exercise early termination rights and a temporary stay in accordance with EC 4.3. In essence, the prohibition to exercise early termination rights is subject to a certain defined period during which it applies, that is 90 days for contracts other than QFCs. For QFCs, a temporary stay applies. As noted above for EC 4.2 and EC4.3, the prohibition and the temporary stay apply, in equivalent terms, to financial companies subject to OLA under Title II and to IDIs subject to receivership under the FDI Act.</p> <p>The identification of the regime applicable to the different types of contracts entered by the firm under resolution (either according to Title II or to the FDI Act) hinges on the definition of QFC¹⁴⁶ This generally includes any securities contract, commodity contract, forward contract, repurchase</p> |

¹⁴⁵ FDI Act, 12 U.S.C. § 1821(e)(13)(C)(i) and 12 U.S.C. § 1821(e)(10)(B).

¹⁴⁶ FDI Act, 12 U.S.C. § 1821(e)(8) (D)(i), and DFA Section 210(c)(8)(D).

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| | <p>agreement, swap agreement, and any similar agreement that the FDIC determines by regulation, resolution, or order to be a QFC for purposes of Title II or the FDI Act, as the case may be.</p> <p>State Insurance. As discussed in greater detail above, the framework governing the early termination of contracts by virtue of commencement of receivership proceedings varies to some degree between states and does not provide for a comprehensive system precluding the exercise of early termination provisions as envisaged in ECs 4.2 and 4.3. In particular, for most states that have implemented the “safe harbor” provisions set out in IRMA and the NAIC’s model provisions, QFCs are expressly excluded from the scope of any stay imposed on the termination of contracts and there is no provision for the imposition of a temporary stay as envisaged in EC4.3.</p> <p>Findings. Both Title II and the FDI Act provide for a prohibition on counterparties of firms under resolution to exercise early termination rights solely as a reason of the commencement of a resolution proceeding or the exercise of resolution powers under Title II or the FDI Act, as the case may be. Such prohibition is subject by a temporary stay period, whose duration differs based on the type of contracts entered into by the firm under resolution (i.e. a QFC or another type of contract). Both Title II and the FDI Act provide for a definition of QFC in order to identify the regime for temporary stay specifically applicable.</p> <p>The state insurance resolution regime does not generally provide for a comprehensive system precluding the exercise of early termination provisions.</p> |
| Assessment of KA4 | |
| Comments | <p>The U.S. legal framework under DFA and the FDI Act provide for adequate arrangements preserving financial stability by disallowing early termination rights solely as a reason of the entry of a firm in resolution, and, where such early termination rights are exercisable, for a limited stay from such rights. That said, the FDI Act could usefully be amended to enable the FDIC to override early termination rights in contracts of subsidiaries and affiliates of an IDI undergoing resolution. While many state insurance resolution regimes have implemented a “safe harbor” provision, they do not provide for a temporary stay on the early termination of financial contracts.</p> |
| 5. Safeguards | |
| <p>KA5.1</p> <p>KA5.2</p> <p>KA5.3</p> <p>KA5.4</p> | <p>Resolution powers should be exercised in a way that respects the hierarchy of claims while providing flexibility to depart from the general principle of equal (pari passu) treatment of creditors of the same class, with transparency about the reasons for such departures, if necessary to contain the potential systemic impact of a firm’s failure or to maximise the value for the benefit of all creditors as a whole. In particular, equity should absorb losses first, and no loss should be imposed on senior debt holders until subordinated debt (including all regulatory capital instruments) has been written-off entirely (whether or not that loss-absorption through write-down is accompanied by conversion to equity).</p> <p>Creditors should have a right to compensation where they do not receive at a minimum what they would have received in a liquidation of the firm under the applicable insolvency regime (“no creditor worse off than in liquidation” safeguard).</p> <p>Directors and officers of the firm under resolution should be protected in law (for example, from law suits by shareholders or creditors) for actions taken when complying with decisions of the resolution authority.</p> <p>The resolution authority should have the capacity to exercise the resolution powers with the necessary speed and flexibility, subject to constitutionally protected legal remedies and due process. In those jurisdictions where a court order is still required to apply resolution measures, resolution authorities should take this into account in the resolution planning process so as to ensure that the time required for court proceedings will not compromise the effective implementation of resolution</p> |

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| | measures. |
| KA5.5 | The legislation establishing resolution regimes should not provide for judicial actions that could constrain the implementation of, or result in a reversal of, measures taken by resolution authorities acting within their legal powers and in good faith. Instead, it should provide for redress by awarding compensation, if justified. |
| KA5.6 | In order to preserve market confidence, jurisdictions should provide for flexibility to allow temporary exemptions from disclosure requirements or a postponement of disclosures required by the firm, for example, under market reporting, takeover provisions and listing rules, where the disclosure by the firm could affect the successful implementation of resolution measures. |
| Essential criteria | |
| EC5.1 | The resolution authority is required to exercise resolution powers in a way that respects the hierarchy of creditor claims under the applicable insolvency regime. |
| Description and findings re EC5.1 | <p>DFA. Title II provides for the following hierarchy of unsecured claims when a financial company is resolved under Title II:</p> <ul style="list-style-type: none"> (i) administrative expenses of the receiver; (ii) any amounts owed to the U.S., unless the U.S. agrees or consents otherwise, and provided that unsecured claims of the U.S. shall, at a minimum, have a higher priority than liabilities of the covered financial company that count as regulatory capital; (iii) certain wages, salaries, or commissions earned by an individual (other than such amounts owed to senior executives or directors of the covered financial company), up to a certain amount and not later than 180 days before the date of the appointment of FDIC as receiver; (iv) certain contributions to employee benefit plans, within specifically defined limits; (v) any general or senior liability of the covered financial company; (vi) any obligation subordinated to general creditors; (vii) wages, salaries, or commissions owed to senior executives or directors of the covered financial company; and (viii) any obligation to shareholders, members, general partners, limited partners, or other persons, with interests in the equity of the covered financial company arising as a result of their status as such.¹⁴⁷ <p>If the FDIC, as receiver for a covered financial company, is unable to obtain unsecured credit or issue unsecured debt for the covered financial company from commercial sources, it may, subject to a court hearing, authorize the obtaining of credit or the issuance of debt by the covered financial company, with priority over any or all obligations of such company.</p> <p>In taking action under Title II, the FDIC shall ensure that the shareholders of a covered financial company shall not receive payments until after all other claims and the OLF are fully paid. The</p> |

¹⁴⁷ DFA Section 210(b)(1)(2) and (3).

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| | <p>FDIC shall ensure that unsecured creditors bear losses, consistent with the above described priority of claims.¹⁴⁸</p> <p>Banking. In the case of the resolution of a IDI, claims against such IDI (other than secured claims to the extent of such security) must be paid pursuant to the following statutory hierarchy of claims, as provided under the FDI Act:</p> <ul style="list-style-type: none"> (i) administrative expenses of the receiver; (ii) any deposit liability of the IDI,¹⁴⁹ (iii) any general or senior liability of the IDI; (iv) any obligation subordinated to depositors or general creditors; and (v) any obligation to shareholders or members arising as a result of their status as shareholders or members (including any depository institution holding company or creditor of such company).¹⁵⁰ <p>The FDIC, in its corporate capacity as administrator of the DIF, may pay claims on accounts of insured deposits in cash from the DIF or transfer such insured deposits to a new IDI.¹⁵¹ In either case, the FDIC, in its corporate capacity, would then be subrogated to all rights of such insured depositors against the failed IDI.¹⁵² The FDIC’s claim as subrogee bears the ranking of a deposit liability under (ii) above.</p> <p>State Insurance. Under state insurance resolution law, the hierarchy of creditor claims is defined explicitly in a case of distribution of assets under a liquidation proceeding. Section 801 of IRMA proposes two alternatives for the hierarchy of creditor claims, each of which divides unsecured claims against the insurer into thirteen classes, and requires that every claim in each class be paid in full or adequate funds retained for their payment before the members of the next class receive payment. No claim by a shareholder, policyholder, or other creditor is permitted to circumvent the priority classes through the use of equitable remedies. While state insurance resolution legislation law does not explicitly provide that the hierarchy of creditor claims in liquidation should be taken into account for purposes of rehabilitation, state insurance receivership laws generally require that creditors be treated fairly and equitably in resolution proceedings and, in the case of a restructuring of liabilities in a rehabilitation proceeding, receive at least as much as they would have received in a liquidation. (See EC 5.3)</p> <p>Findings. Both when it acts as a receiver for a financial company under Title II and for an IDI under the FDI Act, the FDIC is required to exercise resolution powers in a way that respects the hierarchy of creditor claims, as respectively provided thereunder, and that allocates losses to shareholders and unsecured creditors. Likewise, state insurance resolution regimes provide for a clear hierarchy of creditor claims that is taken into consideration both for purposes of liquidation and rehabilitation.</p> |
| EC5.2 | The legal framework requires the resolution authority, as a general principle, to observe the principle of equal (pari passu) treatment of creditors of the same class while permitting departure |

¹⁴⁸ DFA Sections 206(2) and (3), 210(a)(1)(M) and 210(b).

¹⁴⁹ See EC 7.6 for the definition of the term “deposit liability” under the FDI Act.

¹⁵⁰ FDI Act, 12 U.S.C. § 1821(d)(11).

¹⁵¹ FDI Act, 12 U.S.C. § 1821(f).

¹⁵² FDI Act, 12 U.S.C. § 1821(g)(1).

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| | <p>from that principle where it is necessary for either of the following purposes: (i) to protect financial stability by containing the potential systemic impact of the firm's failure; or (ii) to maximise the value of the firm for the benefit of all creditors.</p> |
| <p>Description and findings re EC5.2</p> | <p>DFA. The FDIC as receiver shall treat creditors that are similarly situated under the hierarchy of claims noted above in a similar manner, except that it may treat creditors that are similarly situated in a different manner (including with respect to making payments) if:</p> <ul style="list-style-type: none"> (A) the FDIC determines that such action is necessary: <ul style="list-style-type: none"> (i) to maximize the value of the assets of the covered financial company; (ii) to initiate and continue operations essential to implementation of the receivership or any bridge financial company; (iii) to maximize the present value return from the sale or other disposition of the assets of the failed covered financial company; or (iv) to minimize the amount of any loss realized upon the sale or other disposition of the assets of the covered financial company; and (B) all claimants that are similarly situated under the hierarchy of claims receive not less than what they would have received if the FDIC had not been appointed receiver and the covered financial company had been liquidated under chapter 7 of the Bankruptcy Code or any similar provision of state insolvency law applicable to such company. <p>The above departure does not affect secured claims or secured entitlements in respect of assets or property held by the covered financial company.</p> <p>In addition, the FDIC may, with the approval of the Treasury Secretary, make additional payments or credit additional amounts to any claimant or category of claimants of the covered financial company if it determines that such payments or credits are necessary or appropriate to minimize losses to the FDIC as receiver, provided that (i) no claimant or category of claimants receiving such additional payments or credits would receive more than the face value amount of any proven claim; and (ii) the FDIC shall not be obligated to make such payments or credit to any other claimant or category of claimants.</p> <p>The FDIC has ruled that it would not exercise its discretion under the Dodd-Frank Act to make payments or credit amounts to some creditors but not others similarly situated in a manner that would result in preferential treatment—through recoveries higher than the amount established under the priority of payment—to holders of long-term senior debt (defined as unsecured debt with a term of longer than one year), subordinated debt, or equity, and other holders of general or senior liabilities, except where, with exclusive reference to the latter category, the FDIC through the affirmative vote of a majority the Board of Directors determines that such additional payments or credit amounts to such holders are necessary to achieve the objectives referred to above under (i) to (iv).¹⁵³</p> <p>Banking. The FDIC, in its discretion and in the interests of minimizing its losses, may use its own resources to make additional payments or credit additional amounts to any claimant or category of claimants. The FDIC may make such payments or credit such amounts to an open IDI to induce</p> |

¹⁵³ See the following relevant provisions of DFA: Section 210(b)(4); Section 210(b)(5); Section 210(d)(4). See also 12 C.F.R. § 380.27.

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| | <p>such IDI to accept liability for such claims (for instance, in the context of a purchase and assumption scheme).¹⁵⁴ The FDIC may also take other action or provide assistance for the purposes of winding up an insured depository institution notwithstanding this least cost test if certain financial stability grounds are met (see also under EC 2.2).</p> <p>State Insurance. State insurance resolution regimes generally require the commissioner as receiver to observe the principle of equal treatment of creditors of the same class.</p> <p>Section 801, alternative 1 of IRMA explicitly prohibits the commissioner from creating subclasses within a class. Any deviation from the order of priority set forth therein is regarded as violation of law and the court may not approve such a distribution. Similarly, neither the New York Insurance Law nor the Life and Health Insurers Rehabilitation and Liquidation Act of New Jersey have explicit provisions that allow either the commissioner as receiver or the receivership court as supervisor to depart from the principle of equal treatment within a class.</p> <p>In a liquidation proceeding, a court would not allow a deviation from the equal treatment within a class with a view to protecting financial stability or maximizing the value of the firm, especially when this would materially harm policyholders. In the case of a rehabilitation, IRMA does not explicitly prohibit a rehabilitator from treating creditors within the same class differently but requires a rehabilitation plan approved by the court to be fair and equitable to all parties concerned. It would not appear that this framework would permit deviations from the principle of <i>pari passu</i> treatment, in particular, to protect financial stability by containing the potential systemic impact of the firm's failure. Section 403 E of IRMA allows a rehabilitation plan to designate and separately treat one or more separate sub-classes consisting of those claims within these classes that are for or reduced to <i>de minimis</i> amounts.</p> <p>Findings. Under Title II, while the FDIC is generally required to observe the principle of equal (<i>pari passu</i>) treatment of creditors of the same class, it is also provided with a wide degree of flexibility to permit departure from such principle, in line with EC 5.2.</p> <p>Under the FDI Act, the FDIC as receiver is generally required to observe the principle of equal principle of creditors of the same class. While no provisions explicitly permit a departure from such <i>pari passu</i> treatment, the resolution regime under the FDI Act is designed in such a manner that the FDIC can effectively depart from such principle, either by using DIF resources when necessary to minimize its losses (thus maximizing the value of the firm for the benefit of creditors) or by providing assistance in derogation from the least cost test when that is necessary for financial stability purposes.</p> <p>State insurance resolution laws generally require adherence to the principle of equal treatment of creditors of the same class. Departures from this principle would not be allowed for the purposes of protecting financial stability.</p> |
| <p>EC5.3</p> | <p>The legal framework provides that creditors that receive less as a result of resolution than they would have received in liquidation have a right to compensation. The resolution regime specifies how the right to compensation can be exercised.</p> |
| <p>Description and findings re EC5.3</p> | <p>DFA. Creditors are statutorily required to receive not less than what they would have received had the FDIC not been appointed receiver under Title II of the Dodd-Frank Act and the covered financial company had been liquidated under Chapter 7 of the Bankruptcy Code or any similar</p> |

¹⁵⁴ FDI Act, 12 U.S.C. § 1821(i)(3).

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| | <p>provision of state insolvency law applicable to the covered financial company. The maximum liability of the FDIC shall not exceed such amount.¹⁵⁵</p> <p>Banking. The FDI Act is the applicable resolution regime in all cases for IDIs, in that IDIs are not subject to a bankruptcy or liquidation proceeding under the Bankruptcy Code. However, the FDI Act requires taking into account the counter-factual of the liquidation scenario in determining the maximum liability of the FDIC as receiver or the IDI. Indeed, the maximum liability of the FDIC shall equal the amount a claimant would have received if the FDIC had liquidated the assets and liabilities of the failed IDI without exercising resolution powers (e.g., entailing the transfer to a bridge bank or to another IDI).¹⁵⁶ Moreover, the use of the DIF is aimed to facilitate resolution and the application of the least cost test, thus operating in a manner that seeks to maximize value for creditors.</p> <p>State Insurance. U.S. state insurance receivership laws generally require that creditors be treated fairly and equitably in resolution proceedings and, in the case of a restructuring of liabilities in a rehabilitation proceeding, receive at least as much as they would have received in a liquidation.</p> <p>Section 403 A of IRMA requires that any rehabilitation plan be fair and equitable to all parties concerned, and it provides for no less favorable treatment of a claim or class of claims than would occur in liquidation, unless the holder of particular claim or interest agrees to such less favorable treatment. This provision reflects more general principles of state receivership law that has developed through precedent.</p> <p>As any resolution plan must be approved by a court, state insurance resolution law does not generally provide for (or require) an express right of compensation in cases where this standard is not met.</p> <p>Findings. The “no-creditor worse off safeguard” is incorporated in the U.S. legislation, under both the DFA and the FDI Act. The right of compensation can be exercised according to general principles, by filing a claim against the FDIC as a receiver or seeking judicial review under the Administrative Procedures Act. While the no creditor worse off principle also applies in the rehabilitation of an insurer, the court, through its approval of the rehabilitation plan, ensures that creditors receive at least as much as they would have in liquidation.</p> |
| <p>EC5.4</p> | <p>The legal framework protects the directors and officers of a firm in resolution against liability, including to shareholders and creditors of the firm, arising from actions taken when acting in compliance with decisions and instructions of domestic resolution authorities.</p> |
| <p>Description and findings re EC5.4</p> | <p>DFA. Upon commencement of an orderly liquidation under Title II, the FDIC takes over the assets of and operates the covered financial company with all the powers of the members or shareholders, the directors, and the officers of the company or IDI, and conducts all business.</p> <p>The FDIC may also provide for the exercise of any function by any member or stockholder, director, or officer of any covered financial company for which it has been appointed receiver.</p> <p>Members of the board of directors (or body performing similar functions) of a covered financial company for which the FDIC has been appointed receiver shall not be liable to the shareholders and creditors for acquiescing in or consenting in good faith to the appointment of the FDIC as receiver.¹⁵⁷</p> |

¹⁵⁵ DFA Section 210(a)(7)(B) and (d)(2).

¹⁵⁶ FDI Act, 12 U.S.C. § 1821(i)(2).

¹⁵⁷ DFA Section 207.

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| | <p>Banking. Same considerations made above apply with respect to the FDI Act.</p> <p>State Insurance. Under U.S. state insurance resolution law, the commissioner as receiver effectively takes over the control of the insurer in resolution and assumes the role of directors and officers.</p> <p>For example, Section 17B:32-47a of Life and Health Insurers Rehabilitation and Liquidation Act of New Jersey states that an order to liquidate the business of a domestic insurer shall direct the liquidator to take possession of the assets of the insurer and to administer them under the general supervision of the court, and the liquidator is vested by operation of law with the title to all of the property, contracts and rights of action. Section 402 of IRMA explicitly provides that the authority of directors and officers and managers of the insurer in rehabilitation is suspended upon appointment of rehabilitator. Any director, officer or manager that is not replaced is required to act in compliance with the receiver’s decisions and instructions.</p> <p>While state resolution frameworks do not appear to provide for express protection of directors or officers from liability against shareholders and creditors, for any action taken in compliance with decisions and instructions of commissioner as a resolution authority, any potential for such liability would appear to be minimal.</p> <p>Findings. The circumstance that the FDIC takes over the assets and management of a covered financial company or failed IDI, by operating with all the powers of shareholders, directors and officers should, in principle, shield from liability the directors or officers of such company or IDI that are not replaced. Indeed, since the FDIC is responsible for making all relevant decision for the business of the company or IDI, it would appear that any director or officer that is required to act in compliance with the FDIC’s decisions and instructions would not be at risk of liability. As a state insurance resolution is conducted under the supervision of the court, there is relatively little risk that actions taken in compliance with the court’s decisions will give rise to liability.</p> |
| <p>EC5.5</p> | <p>The legal framework enables the resolution authority to exercise the powers in KA 3 in a timely manner and without any delay that could compromise the achievement of the objectives mentioned in KA 2.3. Where prior court approval is required, the timelines required for completing court proceedings are consistent with KA 5.4 and are incorporated into resolution planning.</p> |
| <p>Description and findings re EC5.5</p> | <p>DFA. In the absence of acquiescence or consent by the board of directors of the covered financial company, the U.S. District Court for the District of Columbia has a statutorily circumscribed role in the appointment of the FDIC as receiver of a financial company under Title II of the Dodd-Frank Act. The court shall decide, on a strictly confidential basis and without prior public disclosure, whether the determination made by the Treasury Secretary that the company is a financial company and is in default or in danger of default is arbitrary and capricious. If the court determines not then it must issue an order immediately authorizing the appointment of the FDIC as receiver. If deemed arbitrary and capricious, the court must instead immediately provide to the Treasury Secretary a written statement of each reason supporting its determination, and afford the Treasury Secretary an immediate opportunity to amend and refile the petition. If the court does not make a determination within 24 hours of receipt of the petition by the Treasury Secretary, liquidation under Title II shall automatically commence.¹⁵⁸ The Court’s determination may be appealed, but there is no stay pending any such appeal. (See also description and findings for EC2.2).</p> |

¹⁵⁸ DFA Section 202(a).

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| <p>Once the FDIC is appointed as receiver, a procedure governs the resolution of claims by the FDIC, which can allow or disallow claims against the covered financial company¹⁵⁹. A judicial determination of claims is provided for, in that a claimant may file suit on a claim in the district or territorial court of the U.S. for the district within which the principal place of business of the covered financial company is located within 60 days of the earlier of (i) the expiration of the period in which the FDIC as receiver must provide notification of allowance or disallowance and (ii) notification by the FDIC as receiver of disallowance of the claim, and such court shall have jurisdiction to hear such claim.¹⁶⁰</p> <p>Except as otherwise provided under Title II, no court shall have jurisdiction over</p> <p>(i) any claim or action for payment from the assets of any covered financial company for which the FDIC has been appointed receiver, including any assets which the FDIC may acquire from itself as such receiver; or</p> <p>(ii) any claim relating to any act or omission of such covered financial company or the FDIC as receiver.¹⁶¹</p> <p>Courts may not restrain or affect the exercise of powers or functions of the FDIC as receiver, except as provided under Title II, and any remedy against the FDIC shall be limited to money damages.¹⁶² No attachment or execution may be issued upon assets in the possession of the FDIC as receiver.</p> <p>Once the FDIC is appointed receiver, no prior court approval is required before the FDIC as the resolution authority takes a resolution action or applies a resolution measure.</p> <p>For a discussion on the commencement of resolution proceeding under Title II with respect to an insurance company, and the related uncertainties, see EC 2.1.</p> <p>Banking. Save as provided under the provisions of the FDI Act, courts may not restrain or affect the exercise of powers or functions of the FDIC as receiver.¹⁶³ No attachment or execution may be issued by any court upon assets in the possession of the FDIC as receiver.¹⁶⁴</p> <p>In addition, except as otherwise provided under the relevant provisions of the FDI Act, no court shall have jurisdiction over</p> <p>(i) any claim or action for payment from, or any action seeking a determination of rights with respect to, the assets of any IDI for which the FDIC has been appointed receiver, including assets which the FDIC may acquire from itself as such receiver; or</p> <p>(ii) any claim relating to any act or omission of such institution or the FDIC as receiver.¹⁶⁵</p> <p>The FDI Act provides for a procedure for a determination of claims and for the judicial determination of claims upon the expiration of the period in which the FDIC as receiver must</p> |
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¹⁵⁹ DFA Section 210 (a) (3).

¹⁶⁰ DFA Sections 210(a)(4)(A) and (B).

¹⁶¹ DFA Section 210(a)(9)(D).

¹⁶² DFA Section 210(e).

¹⁶³ FDI Act, 12 U.S.C. § 1821(j).

¹⁶⁴ FDI Act, 12 U.S.C. § 1821(d)(13)(C).

¹⁶⁵ FDI Act, 12 U.S.C. § 1821(d)(13)(D).

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| | <p>provide notification of allowance or disallowance or upon notification by the FDIC as receiver of disallowance of the claim.¹⁶⁶</p> <p>State Insurance. The state insurance resolution regime is a procedure in which the commissioner as receiver generally takes action only upon prior approval of the court.</p> <p>While it is generally possible for the State commissioner to take control of a failing institution and to receive court approval for the imposition of a stay on enforcement actions very quickly, many other restructuring measures may only be taken (e.g., transfers of assets and liabilities of the company) in the context of a rehabilitation or liquidation plan after appropriate notice to affected parties and, if necessary, a hearing. The KA and the AM acknowledge that “it is not necessarily inconsistent with the KA if the resolution regime makes provision for a court order or confirmation for the exercise of resolution powers to be effective” but note that “it is important to ensure that any requirement for court approval does not impede rapid intervention and the ability to achieve the objectives of resolution.” In providing guidance as to the appropriate standard of speed, EN 5 (e) notes that timely exercise of resolution powers “could be facilitated by a legal framework that provides” for, inter alia, (i) “expedited procedures (for example, with shortened notice, filing and decision deadlines for a appeals)”; and “applications by the resolution authority without notice to the firm or other affected parties”. While courts in the U.S. are highly efficient and generally show a high level of deference to state commissioners, it would not appear that a U.S. insurance resolution authority could always obtain court approval for the exercise of the full range of resolution powers with the necessary speed contemplated by this standard, given the general requirements in state legislation for affected parties to be given adequate notice and a right to be heard. While the KA recognize that the timelines needed for more traditional insurance resolution measures (e.g., timely pay out of policy holders or for run off) may take longer than those envisaged for a bank resolution, the KA do not otherwise differentiate between the timelines needed for the exercise of resolution powers with respect to banks and insurers.</p> <p>Findings. Under Title II, the judicial review of the commencement of the orderly liquidation proceeding is circumscribed to certain well-defined grounds (arbitrariness and capriciousness of two specified determinations). While prior court approval is required in order to commence such proceeding if the firm’s board of directors does not consent or acquiesce to the FDIC’s appointment as receiver, the expedited timeframe would allow the exercise of resolution powers with the necessary speed and flexibility. Likewise, the FDI Act enables the FDIC to exercise its resolution powers in a timely manner. As regards state insurance resolution regimes, the requirements for court approval of resolution actions after notice and a hearing may, in some cases, undermine the timely implementation of necessary resolution measures.</p> |
| EC5.6 | <p>The legal framework provides that the only remedy that can be obtained from a court or tribunal through judicial review of measures taken by resolution authorities acting within their legal powers and in good faith is compensation, to the exclusion of any remedy that could constrain the implementation of, or reverse, any such measure taken by the resolution authority.</p> |
| Description and findings re EC5.6 | <p>DFA. The Dodd-Frank Act expressly limits any remedy against the FDIC to money damages. Moreover, courts may not restrain or affect the exercise of powers or functions of the FDIC as receiver, except as otherwise provided under Title II.¹⁶⁷</p> <p>Banking. The FDI Act does not include an explicit provision similar to the one under the DFA limiting the remedy for claimants to the award of money damages. However, as under DFA, courts</p> |

¹⁶⁶ FDI Act, 12 U.S.C. § 1821(d)(5)(A) and (6).

¹⁶⁷ DFA Section 210(e).

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| | <p>may not restrain or affect the exercise of powers or functions of the FDIC as receiver, except as provided under the FDI Act.¹⁶⁸</p> <p>Upon certain circumstances (such as when the FDIC appoints itself as receiver to prevent losses to the DIF), the IDI may, within 30 days of the FDIC’s appointment as receiver for the IDI, bring an action in the U.S. District Court for the District of Columbia or in the district in which the home office of the IDI is located seeking the removal of the FDIC as receiver.¹⁶⁹ While there are no reported precedents regarding this specific instance, a similar provision exists for federal savings associations:¹⁷⁰ the latter has been the subject of court cases. There have been no recent instances where courts have removed the FDIC as a receiver. The consequences of the possible removal of the FDIC as a receiver—particularly, whether acts by the FDIC could be unwound—may not be easily predicted. Furthermore, the above-mentioned provision according to which courts may not restrain or affect the exercise of powers or functions of the FDIC as receiver is generally relied upon by courts in dismissing challenges to the FDIC’s appointment as receiver. Similar considerations arise when the appointment of the FDIC as receiver is made, with respect to state-licensed banks, by state authorities.</p> <p>State Insurance. The state insurance resolution regime generally requires court approval for all significant resolution measures taken by a receiver. As such, the circumstances in which a receiver’s actions would be taken as an administrative measure subject to ex post judicial review are very limited. Under IRMA, the reversal or modification on appeal of an order of resolution proceedings does not affect the validity of the acts of the receivership pursuant to the order.¹⁷¹</p> <p>Findings. Title II explicitly limits the remedy that can be obtained from a court through judicial review to money damages. No similar limitation exists under the FDI Act; however, courts are prevented from restraining or affecting the exercise of the FDIC powers as receiver. In theory, there exists the possibility—albeit remote—that the FDIC appointment as receiver be removed if a challenge is brought within 30 days of such appointment. While there are no precedents and there are grounds to argue that, in such instance, the actions taken by the FDIC would not be reversed, consideration could be given, along the lines of the DFA provision, to limit the remedy available for compensation arising from resolution measures to the award of money damages.</p> <p>As most actions of a receiver under state resolution law are taken with the prior approval of a court, there are only limited circumstances in which ex post judicial review of administrative actions would be available or needed.</p> |
| EC5.7 | The legal framework allows for temporary exemptions from disclosure requirements, for example, under market reporting, takeover provisions and listing rules, or the postponement of a disclosure, by a firm to be granted in circumstances where that disclosure could affect the successful implementation of resolution measures. |
| Description and findings re EC5.7 | DFA and Banking. As a general matter, under the U.S. regime resolution powers are exercised on a “closed-firm” basis, i.e. upon subjecting a covered financial company to orderly liquidation or an IDI to a receivership. This implies that such company or IDI may no longer typically have audited financial statements and would, in due course, be de-listed from any exchanges on which its securities were traded. Moreover, the FDIC, as receiver, succeeds to all rights, titles, powers, and |

¹⁶⁸ FDI Act, 12 U.S.C. § 1821(j).

¹⁶⁹ FDI Act, 12 U.S.C. § 1821(c)(7).

¹⁷⁰ 12 U.S.C. § 1464 (d) 2

¹⁷¹ IRMA Section 205G.

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| | <p>privileges of the covered financial company or IDI, and the rights and claims of shareholders and creditors against the assets of the company or IDI are terminated by statute once the firm enters resolution, except for their right to payment, resolution, or other satisfaction of their claims.</p> <p>Firms under resolution remain subject to SEC reporting requirements (8-K, 10-K and 10-Q) under the Securities Exchange Act of 1934, but relief may be available in certain circumstances. The SEC has discretion to accept modifications to the reporting requirements, similar to the modified reporting it accepts from companies undergoing a reorganization or bankruptcy process.</p> <p>With respect to the FDI Act, given that the issuers of financial instruments are generally BHCs, disclosure requirements tend not to apply to IDIs. When a BHC is subject to a bankruptcy proceeding, such as in the context of an IDI receivership, the SEC may accept modifications to the reporting requirements, by accepting the monthly reports normally filed with the bankruptcy courts.</p> <p>The implementation of resolution powers under DFA under the SPE may raise additional complications, given the envisaged timeframe for the valuation of the bridge company’s financial situation, the related reporting, registration and accounting framework, and the process for the conversion of claims into securities in a new holding company. The FDIC and the SEC are working to establish appropriate standards that would apply in such context.</p> <p>Foreign firms issuing securities in the U.S. are subject to reporting requirements and must file an annual report on Form 20-F and reports on Form 6-K. Eligible foreign firms under resolution could terminate reporting by going through a de-registration process. The SEC can also accept modifications to reporting requirements by accepting disclosure requirements applicable under foreign insolvency laws.</p> <p>State Insurance. No specific issues arise with respect to state insurance resolution regimes. In the U.S., insurance companies are subject to market reporting, takeover provisions, listing rules, or securities disclosure requirements to a lesser extent than their holding companies and banks.</p> <p>Findings. The U.S. regime does not explicitly contemplate an exemption from disclosure requirements applying to firms under resolution. The circumstance that a covered financial company or IDI is resolved on a “closed-firm basis” may mitigate concerns deriving from disclosures that can affect the successful implementation of resolution measures, as the resolved firm is no longer operating on a going concern basis. The SEC has also discretion to accept modifications from disclosure requirements applicable under the Securities Exchange Act, and typically exercises such discretion when firms undergo a reorganization and bankruptcy process. Possibly similar conclusions may arise for insurance companies.</p> <p>The implementation of a Title II liquidation may bear additional complexities, given that a holding company will typically be the issuer of securities and that the liquidation process will be protracted over a certain period. It is recommended that the U.S. authorities (such as the FDIC, the SEC, and stock exchanges) continue to work to identify whether the disclosure requirements that would be applicable to a firm in resolution in line with EC 5.7 would warrant acceptance of modified reporting. This would facilitate adequate preparedness where a Title II liquidation is commenced.</p> |
| <p>Assessment of KA5</p> | |
| <p>Comments</p> | <p>The exercise of resolution powers is subject to safeguards and due process requirements in line with KA 5. The U.S. resolution regime under DFA and FDI Act also provides for the necessary flexibility to take speedy action, in the interest of financial stability and for the preservation of the value of the resolved firm. While state insurance resolution regimes are in line with several features outlined under KA 5, they do not permit a departure from the principle of equal treatment of creditors based on financial stability grounds and, given the</p> |

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| | significant role of the courts in insurance receivership, the timelines of resolution action is likely to be a concern in circumstances where quick action is required. |
| 6. Funding of Firms in Resolution | |
| KA6.1 | Jurisdictions should have statutory or other policies in place so that authorities are not constrained to rely on public ownership or bail-out funds as a means of resolving firms. |
| KA6.2 | Where temporary sources of funding to maintain essential functions are needed to accomplish orderly resolution, the resolution authority or authority extending the temporary funding should make provision to impose any losses incurred on (i) shareholders and unsecured creditors subject to the “no creditor worse off than in liquidation” safeguard (see Key Attribute 5.2); and recover them (ii) if necessary, from the financial system more widely. |
| KA6.3 | Jurisdictions should have in place privately-financed deposit insurance or resolution funds, or a funding mechanism with ex post recovery from the industry of the costs of providing temporary financing to facilitate the resolution of the firm. |
| KA6.4 | Any provision by the authorities of temporary funding should be subject to strict conditions that minimise the risk of moral hazard, and should include the following: (vi) a determination that the provision of temporary funding is necessary to foster financial stability and will permit implementation of a resolution option that is best able to achieve the objectives of an orderly resolution, and that private sources of funding have been exhausted or cannot achieve these objectives; and (vii) the allocation of losses to equity holders and residual costs, as appropriate, to unsecured and uninsured creditors and the industry through ex-post assessments, insurance premium or other mechanisms. |
| KA6.5 | As a last resort and for the overarching purpose of maintaining financial stability, some countries may decide to have a power to place the firm under temporary public ownership and control in order to continue critical operations, while seeking to arrange a permanent solution such as a sale or merger with a commercial private sector purchaser. Where countries do equip themselves with such powers, they should make provision to recover any losses incurred by the state from unsecured creditors or, if necessary, the financial system more widely. |
| Essential criteria | |
| EC6.1 | The legal framework establishes arrangements to provide temporary financing to support the use of the resolution powers set out in KA 3, which include one or a combination of the following: (i) a privately funded resolution fund; (ii) a privately funded protection scheme (for example, for deposits or insurance policy holders); (iii) a privately funded fund with combined deposit or policy holder protection and resolution functions; (iv) recourse to public funds, coupled with a mechanism for recovery from the industry of any losses incurred in the provision of public funds. |
| Description and findings | DFA. The DFA provides a mechanism, the OLF, for the provision of temporary public funding to support the resolution of a failed covered financial company. ¹⁷² This may serve as a temporary source of liquidity in the event that private-sector funding cannot be obtained. FDIC's borrowing |

¹⁷² DFA Section 210(n).

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| re EC6.1 | <p>in connection with the liquidation of a covered financial company may not exceed (i) an amount equal to 10 percent of the total consolidated assets of the company during the first 30 days of the receivership, followed by (ii) an amount equal to 90 percent of the fair value of the total consolidated assets of the company that are available for repayment, once this has been calculated by the FDIC. The FDIC and U.S. Treasury issued a joint rule¹⁷³ regarding the calculation of the maximum obligation limitation, which sets out a broad interpretation of total consolidated assets available for repayment that, for example, includes secured assets. The Treasury Secretary may not purchase any obligations unless there is an agreement between him and the FDIC that provides a specific plan for repayment of such borrowing and that demonstrates that the FDIC's income from the assets of the covered financial company and assessments on eligible financial companies will be sufficient to amortize the borrowings within a specified time period. For details on recovering OLF borrowings see EC 6.2.</p> <p>It is unclear whether OLF could be used to provide assistance in connection with the resolution of a covered insurance company under state insurance resolution law. Section 210(n) DFA provides that the OLF will be available with regard to a covered financial company for which the FDIC is appointed receiver. As noted in the discussion of EC 1.1 above, it is unclear whether there are circumstances in which the FDIC could be appointed receiver of a covered insurance company and accordingly, whether the OLF could be used to support such a resolution.</p> <p>Banking. The legal framework in the U.S. establishes a Deposit Insurance Fund (DIF), funded on an ex-ante basis by assessments on IDIs.¹⁷⁴ The DIF may be used by the FDIC in connection with resolution of, and deposit insurance payouts associated with, IDIs. In using the DIF, the FDIC must generally exercise its authorities on a least cost basis.¹⁷⁵ In addition the FDIC has standing authority to borrow \$100 billion from the U.S. Treasury if necessary for deposit insurance purposes¹⁷⁶ to be repaid through assessments on IDIs. The DIF was fully depleted during the crisis before the FDIC substantially increased assessments on the industry in a pro-cyclical way (by requiring all solvent IDIs to pre-pay an estimated three year's deposit insurance premiums) and the DFA increased the minimum reserve ratio and removed a hard cap previously in place (first at 1.25 percent and then raised just prior to the crisis to 1.5 percent of insured deposits) giving the FDIC discretion to set a higher target. The FDIC Board subsequently set a target of 2 percent, that on current assessment rates this will not be reached before 2027. The DFA changed the assessment base from average total domestic deposits to average total consolidated assets minus average tangible equity. In addition, the FDIC changed its methodology for calculating risk based assessments on large and complex banks. These were introduced in light of the requirements in the DFA to offset the impact on small and medium-sized banks that rely primarily on deposits for funding, to large banks with multiple funding sources, as well as experience during the crisis that the credit ratings of large banks did not keep track with the</p> |
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¹⁷³ 12 CFR 380.10.

¹⁷⁴ As of December 31, 2014, the DIF had a fund balance of US\$62.8 billion. The DIF's ratio of reserves to estimated insured deposits as of September 30, 2014, was 0.89 percent.

¹⁷⁵ FDI Act, 12 U.S.C. § 1823(c)(4). The least cost requirement does not apply if the Treasury Secretary, in consultation with the President of the U.S. and upon a recommendation of both the FRB and the FDIC (based on a 2/3 vote by both the FRB and the Board of Directors of the FDIC, determines that compliance with the least cost requirement would have serious adverse effects on economic conditions or financial stability in the US and other action or assistance would avoid or mitigate such adverse effects. FDI Act, 12 USC. § 1823(c)(4)(G).

¹⁷⁶ FDI Act, 12 USC. § 1824(a)(1). The FDIC is also authorized to borrow on behalf of the DIF from the Federal Financing Bank and the Federal Home Loan Banks, FDI Act 12 USC. § 1824(b) and (e).

risks they presented to the DIF.

State Insurance.: A nationwide system of state guaranty funds (GF) exists to provide protection of policy holders of financially- troubled insurance companies. Generally, state GAs (life and health) and state guaranty funds (GF) (property and casualty) are private not-for-profit statutory entities that administer the resources of the guaranty system. Most states have separate GA for life and health insurance, and funds for property and casualty insurance. The NAIC has developed model legislation for GAs/GFs in the areas of property and casualty insurance, and life and health insurance.

The insolvency of an insurance company can potentially implicate the guaranty system in all 50 states. Generally, a finding of insolvency and an order of liquidation of an insurer by the court in the domiciliary state will, by statute in each state, trigger an obligation of each GF or GA to provide coverage under relevant policies for residents of that state; limits on coverage will be defined by legislation in each state. The costs associated with such payouts are recouped from the proceeds of liquidation of the estate and, if necessary, ex post assessments imposed on GAs/GFs members (see below). In the case of life and health insurance, it is open to the GA to provide resources to the receiver to fund a transfer of policies to a healthy acquirer or to provide guaranties for this purpose. In determining whether to provide such funding, the GAs will assess the potential costs of making payments on the policies over time against the cost of funding a transfer to a healthy acquirer.

Two nationwide associations—the NOHLGA and the National Conference of Insurance Guaranty Funds—play an important role in coordinating the response of state GA in an insolvency.

Two issues arise from the operation of this system in the context of the resolution of a systemically important insurance company. First, while the GAs/GFs are legally required to provide coverage in the event of an *insolvency* and liquidation of an insurance company, life and health GAs are permitted but not required to provide funding in the event of a receivership that does not involve a finding of insolvency and order of liquidation (property and casualty guaranty funds do not have this flexibility). While it would be open to life and health GAs to help fund a portfolio transfer, GAs have traditionally been very reluctant to provide financing in such circumstances, and, if they were to do so, the provision of financing would need to be agreed and coordinated between the GAs of the relevant states. Accordingly, it is doubtful that the guaranty system would be available to finance the exercise of resolution powers before the point of insolvency. In addition any such provision would only be for the purposes of policy holder protection, without being available to meet wider resolution objectives, such as supporting resolution as needed to preserve financial stability (KA 2.3).

Second, it would need to be considered whether the financial capacity of the GAs/GFs would be sufficient to address the failure of a systemically important insurer (while recognizing other potential funding sources, including the assets of the estate and borrowing capacity of the guaranty system)—including in light of the system’s reliance upon ex post funding. Beyond their ability to recoup their costs from proceeds of the liquidation and assessments of members, GAs are able to borrow from commercial banks; in this regard, the life and health GA currently report a borrowing capacity of about \$10 billion per year, but not from the public sector.

Findings: The legal framework provides for temporary recourse to public funds, coupled with a mechanism for ex post recovery from the financial industry, with respect to covered financial companies. It also establishes a deposit insurance fund, funded privately on an ex ante basis, with combined deposit protection and resolution functions for failed IDIs. The GAs and GFs are only required to disburse in the event of insolvency and the issuance of a liquidation order for the narrow purposes of policy holder protection. While GAs are permitted to provide funding to support the use of resolution powers before the point of insolvency, it is doubtful that they

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| | would do so. |
| EC6.2 | <p>If the resolution regime provides for the provision of temporary recourse to public funds under point (iv) of EC 6.1, it also ensures that such financing is made available only if:</p> <p>(i) it has been assessed as necessary for financial stability by supporting the implementation of a resolution option that best achieves the statutory objectives of resolution (see KA 2.3);</p> <p>(ii) private sources of funding have been exhausted or would not achieve those objectives; and</p> <p>(iii) losses are allocated to shareholders and, as appropriate, to unsecured and uninsured creditors (in accordance with the hierarchy of claims) and, if necessary, public funds are recovered from the financial industry through assessments or other mechanisms.</p> |
| Description and findings re EC6.2 | <p>DFA. The DFA provides the FDIC as receiver for covered financial companies with discretion to determine that the use of borrowings from the OLF is necessary or appropriate.¹⁷⁷ In exercising such discretion, the FDIC as receiver is bound by the statutory objectives of the FDIC’s resolution authority under Title II to resolve failing financial companies that pose a significant risk to the financial stability of the U.S. in a manner that mitigates such risk and minimizes moral hazard, and to do so in a manner that best fulfills such purpose, so that:</p> <ul style="list-style-type: none"> • creditors and shareholders will bear the losses of the financial company; • management responsible for the condition of the financial company will not be retained; and • the FDIC and other appropriate agencies will take all steps necessary and appropriate to assure that all parties, including management, directors, and third parties, having responsibility for the condition of the financial company bear losses consistent with their responsibility, including actions for damages, restitution, and recoupment of compensation and other gains not compatible with such responsibility.¹⁷⁸ <p>Furthermore, the DFA requires that in taking action under Title II, including the provision of temporary public funding, the FDIC as receiver must determine that such action is necessary for purposes of the financial stability of the U.S. and not for the purpose of preserving the financial company.¹⁷⁹ As discussed in detail in the FDIC’s Notice entitled “Resolution of Systemically Important Financial Institutions: The Single Point of Entry Strategy,” published in the Federal Register on December 18, 2013,¹⁸⁰ the FDIC intends to maximize the use of private sector sources of funding. Only if such sources are unavailable would the FDIC utilize the OLF provided for under Title II as a temporary back-up source of liquidity.¹⁸¹</p> <p>The DFA provides that any borrowings from the OLF, are to be treated as administrative expenses of the FDIC as receiver or amounts owed to the U.S. under the statutory creditor hierarchy,¹⁸² are to first be repaid from recoveries on the assets of the failed financial</p> |

¹⁷⁷ DFA Section 204(d).

¹⁷⁸ DFA Section 204(a).

¹⁷⁹ DFA Section 206(1).

¹⁸⁰ Federal Register 78, F. R. 76614 (December 18, 2013).

¹⁸¹ *Id.* at 76616.

¹⁸² DFA Section 204(d).

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| | <p>company,¹⁸³ which would reduce the recoveries of junior classes of claimants in accordance with the statutory hierarchy of claims. If recoveries are insufficient to repay funds borrowed from the OLF, the FDIC must impose assessments on any claimant that received additional sums, except for payments necessary to initiate and continue operations essential to the implementation of the receivership or any bridge financial company, than what they would have received in liquidation.¹⁸⁴ However, such payments seem unlikely to be made in practice by the FDIC unless in error.</p> <p>By law, taxpayers shall bear no losses from the exercise of any authority under Title II of the DFA.¹⁸⁵ To the extent that recoveries are insufficient to repay borrowers from the OLF, the FDIC would impose risk-based assessments on BHCs with total consolidated assets equal to or greater than \$50 billion; financial companies with total consolidated assets equal to or greater than \$50 billion; and NBFC supervised by the FRB.¹⁸⁶ Title II requires the FSOC to issue a recommendation on the calibration of the assessments and for the FDIC to issue implementing regulations, in consultation with the Treasury Secretary. To date, such regulations have not been prepared.</p> <p>Banking. The FDIC has the authority under the FDI Act to borrow from the U.S. Treasury if necessary for deposit insurance purposes.¹⁸⁷ Any borrowings from the U.S. Treasury are obligations of the Deposit Insurance Fund (DIF) to be repaid by levying open IDIs.¹⁸⁸ The FDIC would only borrow from the U.S. Treasury if the DIF were insufficient to meet claims or contingent claims. The DIF went into deficit during the last crisis as the number of banks closed or supported by the FDIC substantially increased. While the largest cases by asset size (Bank of America, Citibank and Washington Mutual) ultimately did not incur losses for the DIF, the number and cost of failures of small and medium sized banks were sufficient to exhaust the fund.¹⁸⁹ The DIF reached an \$8.2 billion deficit by end September 2009, and the FDIC adopted a DIF Restoration Plan which included applying a one-off mid-year assessment, and mandating banks to pay an estimated three years of deposit insurance premiums in advance. The FDIC's line of credit from the U.S. Treasury was also increased from \$30 to \$100 billion, but not drawn. The requirements in the FDI Act for resolutions to be least cost (unless a systemic risk exception is applied) in effect mean that losses would be allocated to shareholders and as appropriate unsecured and uninsured creditors.</p> <p>State Insurance.: GF do not have access to public funds, although it is an open question (see EC 6.1) as to whether a GA would have access to the OLF pursuant to § 210 (n) DFA.</p> <p>Findings. The resolution regime under the DFA and FDI Act provides for the provision of temporary recourse to public funds under point (iv) of EC 6.1, and broadly ensures that such financing is made available only if necessary and broadly under the circumstances specified in EC 6.2. Insurance GA/GF do not have recourse to public borrowing. To date, the FDIC has not issued implementing rules on risk-based assessments.</p> |
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¹⁸³ DFA Section 210(n)(9)(B)(i).

¹⁸⁴ DFA Section 210(o)(1)(D)(i).

¹⁸⁵ DFA Section 214(c).

¹⁸⁶ DFA Section 210(o)(1)(D)(ii).

¹⁸⁷ FDI Act, 12 USC. § 1824(a)(1).

¹⁸⁸ FDI Act, 12 USC. § 1824(c)(1)(B).

¹⁸⁹ Between January 2008 and September 2009, 120 banks failed, with the most costly for the DIF being Indymac (US\$13.1 billion), BankUnited (US\$5.7 billion) and Colonial Bank (US\$4.5 billion).

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| EC6.3 | If the resolution regime includes the option of placing a firm under temporary public ownership as part of a resolution action, such an option is subject to the following conditions: (i) the failure of the firm, or its resolution through all other options, would cause financial instability; and (ii) there are clear rules regarding the allocation of losses to shareholders and creditors or, if necessary, recovery from financial system participants more widely. |
| Description and findings re EC6.3 | Findings. The resolution regime in the United States does not include the option of placing a financial firm, including IDIs and insurance companies, under temporary public ownership as part of a resolution action. |
| Assessment of KA6 | |
| Comments | The OLF and DIF arrangements are available to provide temporary financing to support the KA3 resolution powers. These arrangements include mechanisms for temporary recourse to public funds and ensure that such financing is only afforded in limited circumstances. The GAs/GFs are only required to disburse in the event of insolvency for the narrow purposes of policy holder protection. While life and health guaranty associations have the discretion to disburse at any earlier state, it is doubtful that they would be available to provide temporary financing, before the point of insolvency, to support the resolution powers set out in KA 3. |
| 7. Cross-border Cooperation | |
| KA 7.1 | The statutory mandate of a resolution authority should empower and strongly encourage the authority wherever possible to act to achieve a cooperative solution with foreign resolution authorities. |
| KA7.2 | Legislation and regulations in jurisdictions should not contain provisions that trigger automatic action in that jurisdiction as a result of official intervention or the initiation of resolution or insolvency proceedings in another jurisdiction, while reserving the right of discretionary national action if necessary to achieve domestic stability in the absence of effective international cooperation and information sharing. Where a resolution authority takes discretionary national action it should consider the impact on financial stability in other jurisdictions. |
| KA7.3 | The resolution authority should have resolution powers over local branches of foreign firms and the capacity to use its powers either to support a resolution carried out by a foreign home authority (for example, by ordering a transfer of property located in its jurisdiction to a bridge institution established by the foreign home authority) or, in exceptional cases, to take measures on its own initiative where the home jurisdiction is not taking action or acts in a manner that does not take sufficient account of the need to preserve the local jurisdiction's financial stability.* Where a resolution authority acting as host authority takes discretionary national action, it should give prior notification and consult the foreign home authority. |
| KA7.4 | 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. The treatment of creditors and ranking in insolvency should be transparent and properly disclosed to depositors, insurance policy holders and other creditors. |
| KA7.5 | Jurisdictions should provide for transparent and expedited processes to give effect to foreign resolution measures, either by way of a mutual recognition process or by taking measures under the domestic resolution regime that support and are consistent with the resolution measures taken by the foreign home resolution authority. Such recognition or support measures would enable a foreign home resolution authority to gain rapid control over the firm (branch or shares in a subsidiary) or its assets that are located in the host jurisdiction, as appropriate, in cases where the firm is being resolved under the law of the foreign home jurisdiction. Recognition or support of |

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| <p>KA7.6</p> | <p>foreign measures should be provisional on the equitable treatment of creditors in the foreign resolution proceeding.</p> <p>The resolution authority should have the capacity in law, subject to adequate confidentiality requirements and protections for sensitive data, to share information, including recovery and resolution plans (RRPs), pertaining to the group as a whole or to individual subsidiaries or branches, with relevant foreign authorities (for example, members of a CMG), where sharing is necessary for recovery and resolution planning or for implementing a coordinated resolution.</p> <p>KA 7.7 Jurisdictions should provide for confidentiality requirements and statutory safeguards for the protection of information received from foreign authorities.</p> <p>* This should not apply where jurisdictions are subject to a binding obligation to respect resolution of financial institutions under the authority of the home jurisdiction (for example, the EU Winding up and Reorganisation Directives).</p> |
| <p>Essential criteria</p> | |
| <p>EC7.1</p> | <p>The legal framework does not create any material barriers to cooperation with foreign resolution authorities, including by providing for automatic action as a result of official intervention or the initiation of resolution or insolvency proceedings in other jurisdictions that could undermine a cooperative solution.</p> |
| <p>Description and findings re EC7.1</p> | <p>DFA. The FDIC, as receiver for a covered financial company, is required to coordinate, to the maximum extent possible, with the appropriate foreign financial authorities regarding the orderly liquidation of any covered financial company that has assets or operations in a country other than the U.S.¹⁹⁰</p> <p>Banking. No provision similar to the one under DFA, noted above, exists under the FDI Act. While the FDI Act does not create any material barriers to cooperation with foreign resolution authorities, the FDIC is not required to take into account the impact of the resolution measure taken by the FDIC on financial stability in the relevant foreign jurisdictions.</p> <p>U.S. branches. As noted under EC 1.2, federal and state-licensed uninsured branches of foreign firms are subject to different, specific resolution regimes.¹⁹¹</p> <p>Under the IBA, the authority to operate a federal branch shall terminate, on an automatic basis, when the parent foreign bank is dissolved or its authority or existence is terminated or cancelled in its country. Upon such termination, the OCC may appoint a receiver, who will take possession of all the property and assets of the foreign bank in the U.S. The OCC may exercise this power also when any creditor obtains a judgment arising from a transaction with the federal branch and such judgment has remained unpaid for thirty days, as well as whenever it becomes satisfied that the foreign bank is insolvent or other grounds broadly related to the financial soundness of the foreign bank or the branch are met. The proceeds from the receivership process shall be returned to the foreign bank’s home office only after all depositors and creditors who have transacted with the U.S. branches have been satisfied. The OCC has never exercised its receivership authority under the IBA. The OCC may also, alternatively, appoint a conservator, having all the powers to operate the bank, or may choose to dissolve or liquidate the branch under the national bank voluntary dissolution provisions.</p> <p>The resolution regime for state-licensed branches of foreign firms varies across states. Under the</p> |

¹⁹⁰ DFA Section 210(a)(1)(N).

¹⁹¹ For the federal regime, see, among other provisions, Section 4(i) and 4(j) of the IBA and the Bank Conservation Act (12 US Code § 206). For the NY regime, see, among other provisions: N.Y. Banking. Law Article 2 §14 1(p); Article 5 §206; Article 13 §606; Articles 13 §618(a), §618-a and 634.

New York Banking Law, when a foreign banking corporation is dissolved or its authority or existence is terminated or cancelled in its jurisdiction, a certificate is required to be filed with the Superintendent of the Department of Financial Services (the "Superintendent"), and the filing has the same effect as a revocation of the license. The Superintendent may, in his discretion, take possession of the business and property in New York (NY) of a foreign banking corporation upon a variety of grounds, including when the license of such corporation has been revoked under the above mentioned circumstances, when unsound and unsafe conditions exist, or when there is reason to doubt its ability to pay in full the claims of creditors of the NY branch. Once it takes possession, the Superintendent shall liquidate or deal with such business and property in accordance with the liquidation regime. Proceeds of the liquidation go first to pay the claims of creditors arising from the transaction of business with the NY branch. After claims against the branch are satisfied, any excess proceeds are paid over, upon court order, to any liquidators of the foreign bank's other U.S. branches or offices. Only after such claims are satisfied are any remaining proceeds returned to the principal office of the foreign bank.

State Insurance. State insurance commissioners are given broad authority to share information with foreign supervisors and resolution authorities where adequate confidentiality arrangements are in place. Moreover, state insurance commissioners in some states may commence conservatorship proceedings with respect to the assets of a non-U.S. insurer not domiciled in the relevant jurisdiction. However, there is nothing that requires state insurance commissioners to cooperate with their foreign counterparts.

While there are no automatic "triggers" that require a state commissioner to commence receivership proceedings against a foreign branch in particular circumstances—for example, if the parent is subject to foreign resolution proceedings or has lost its license in the home jurisdiction—the framework for liquidation effectively relies upon the ring-fencing of assets for the satisfaction of the claims for the branch's creditors. The rehabilitation or liquidation of a foreign insurer's U.S. branch in its "state of entry" will be conducted as if the branch were a separate legal entity; in the case of liquidation, the assets of the branch will need to be distributed to satisfy the claims of the branch's creditors. Foreign branches, as a condition for entry into the state, will be often required to put in place "trusteed assets" that will be used to satisfy claims of the branch's creditors in liquidation.

Findings. While no material barriers to cooperation are provided under the DFA and the FDI Act, the FDI Act contains no reference to cooperation requirements with foreign authorities. The DFA includes a cooperation mechanism, but this applies only with respect to the commencement of a Title II proceeding in the U.S. and does not reflect the possibility that a resolution proceeding be commenced in a foreign jurisdiction. It may not be fully clear how the duty of cooperation for the FDIC could be interpreted, given its broader mandate as a resolution authority as examined under KA 2 above and the circumstance that the triggers of a resolution under Title II refer to the effects of resolution actions on financial stability in the U.S. It is therefore recommended that the cooperation requirements under the DFA be appropriately clarified and broadened in light of the above and that a similar mechanism be added under the FDI Act

The regime for federal and state-licensed uninsured branches may also undermine a cooperative solution. In general, the powers of the OCC or the state banking authorities (such as the Superintendent) are discretionary in nature. While, under the IBA or applicable state law, insolvency or resolution proceedings would automatically result in the termination of the authority to operate the branch or agency, the OCC or state authority, as the case may be, would have some discretion in handling the wind-down of the branch or agency, which may entail the receivership of the branch or agency as one of the more likely outcomes. In such event, the OCC (or the receiver appointed by it) and the state authorities have a statutory responsibility to protect the interests of the creditors of the U.S. uninsured branches. This may lead them to

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| | <p>taking action aimed at preserving the assets of the U.S. uninsured branches to the primary satisfaction of such creditors and to the possible detriment of a cooperative solution.¹⁹² (See also EC 7.2). A cooperative solution may also be undermined by state insurance receivership frameworks, where the provisions governing the liquidation of a foreign branch in a manner that requires its assets to be used for the benefit of the branch's creditors are a material barrier to cooperation. It is recommended that the relevant frameworks for both banking and insurance resolution, as reflected in the above-mentioned legal provisions, be amended to require the authorities involved in the resolution of a systemic U.S. uninsured branch of a foreign firm to cooperate with the competent foreign resolution authority (See also recommendations under KA 1).</p> <p>Moreover, the provisions of the IBA and relevant state laws seem outdated and prone to possible conflicting interpretations. Should the commencement of a resolution proceeding in the home country qualify as a "cancellation or termination"—as these terms are used in the IBA or in the NY Banking Law—the mandatory consequence would be the revocation of the bank license. Such automatic action would be in conflict with EC 7.1.</p> |
| EC7.2 | <p>The legal framework of the jurisdiction under review establishes clear and transparent mechanisms or processes through which actions by a foreign resolution authority can be given prompt legal effect in the jurisdiction under review, either by way of recognition or by taking supportive measures under the domestic resolution regime. Those mechanisms or processes are sufficient to enable such legal effect to be achieved whatever the form of a foreign firm's establishment or operations in the jurisdiction under review (for example, subsidiary, branch or only assets within the jurisdiction) and, where a firm is being resolved under the law of a foreign jurisdiction, enable the foreign resolution authority to gain rapid control over the firm (branch or shares in a subsidiary) or its assets that are located in the jurisdiction under review.</p> |
| Description and findings re EC7.2 | <p>General considerations. Under the U.S. regime, the primary tool for the recognition of foreign insolvency proceedings is represented by Chapter 15 of the Bankruptcy Code, which draws upon the Model Law on Cross-Border Insolvency as promulgated by the United Nations Commission on International Trade Law. While foreign proceedings will not be recognized under Chapter 15 if they are considered as "manifestly contrary to the public policy of the United States", it should be noted that this public policy exception—which also draws upon the above-mentioned Model Law—has been narrowly interpreted by U.S. courts. However, as foreign banks with a branch or agency in the United States are not eligible for recognition under Chapter 15¹⁹³ Chapter 15 is relevant only in a more limited subset of circumstances respecting banks. In the context of insurance, while Chapter 15 generally applies to resolution measures respecting foreign insurance companies, it excludes certain security arrangements established under state insurance laws by foreign insurance companies. It is therefore necessary to distinguish different situations, as follows.</p> <p>Chapter 15 of the Bankruptcy Code. Chapter 15 may be relevant in a variety of circumstances involving the operations of a foreign bank in the U.S. Such a bank may have assets or liabilities in the U.S. or governed by U.S. law. In these circumstances, Chapter 15 may represent the avenue</p> |

¹⁹² A cooperative solution was put in place recently in the context of the resolution proceeding of Banco Espírito Santo (BES), governed by Portuguese law. While Banco Espírito Santo had a NY branch, the Superintendent did not make use of its resolution powers and approved the license of a new branch, owned by the bridge bank which acquired certain assets and liabilities of BES. It should be noted, however, that the creditors of the NY branch did not incur any loss in such proceeding.

¹⁹³ 11 USC. § 109 (b) and 11 USC. § 1501(c)(1).

through which a foreign resolution authority could obtain recognition of a foreign resolution measure in the U.S., provided that such measure comports with principles of fairness, and subject to what noted below with respect to the action of the local authorities.¹⁹⁴ Moreover, although, as noted above, foreign resolution proceedings of foreign banks with branches or agencies in the United States would not be eligible for recognition under Chapter 15, a U.S. court may, in theory, proceed to recognize a foreign proceeding in accordance with judicial principles of comity and based on the principles enshrined in Chapter 15.

Chapter 15 may also provide an avenue for the recognition of resolution measures adopted by a foreign resolution authority in respect of a foreign insurer although its use in the context of insurance has been, up to now, rare. However, Chapter 15 precludes a court from granting relief with respect to any deposit, escrow or trust fund or security required or permitted under any applicable state insurance law or regulation. This exclusion relates primarily to arrangements under which certain foreign insurers (e.g., reinsurers) write reinsurance to cover U.S. insurers, or insurance to cover U.S. risks on a surplus lines basis and to post collateral in a trust for U.S. ceding insurers or claimants under U.S. insurance policies. Exclusion from the scope of Chapter 15 is designed to preclude a court under Chapter 15 from upsetting these arrangements. This approach effectively amounts to the ring-fencing of the assets held in trust for the benefit of U.S. stakeholders. Chapter 15 will also be of limited use in circumstances where the foreign insurer—for example, a U.S. branch of the insurer—is the subject of a state receivership proceeding. In such circumstances, a U.S. court will be very reluctant to grant relief in a manner that is inconsistent with the U.S. receivership.

Upon filing the petition for recognition in a bankruptcy court, the foreign representative of a foreign insolvency proceeding may request, and the bankruptcy court may grant, provisional relief where such relief is urgently needed to protect the assets of the debtor or the interests of the creditors. Federal and state courts are required to grant comity or cooperation to the foreign representative. However, courts may refuse to take any action under Chapter 15 if the action would be “manifestly contrary to the public policy of the U.S.” Upon recognition of the foreign proceeding, the court may entrust the distribution of the debtor’s assets to the foreign representative or another person, provided that it is satisfied that the interests of creditors in the U.S. are sufficiently protected. While there is a tradition of U.S. courts recognizing foreign insolvency proceedings under principles of comity, the standards for the recognition under Chapter 15 of a foreign resolution proceeding of a bank or insurer are not clearly defined.¹⁹⁵

In the context of the possible strengthening of the cross-border resolution regime in the U.S., proposals have been made to revise Chapter 15 of the Bankruptcy Code to cater for its application to U.S. branches; alternatively, a general policy statement could be issued by the U.S. authorities clarifying that actions taken by foreign resolution authorities would be supported and enforced under principles of comity, provided that financial stability in the U.S. is preserved.

DFA. The DFA provides limited means through which actions by a foreign resolution authority can be given prompt legal effect, either by way of recognition or by taking supportive measures, under the U.S. resolution regime. While the DFA does not provide for recognition, the FDIC, as receiver for a covered financial company, is required to coordinate, to the maximum extent

¹⁹⁴ 11 USC. § 1501 *et seq.* Several complex issues may be relevant in this respect, including whether contractual agreements provided for the consent to certain actions taken by foreign resolution authority.

¹⁹⁵ In a recent case, a US court has recognized the resolution proceeding of Irish Bank Resolution Corp., governed by Irish law, as a foreign main proceeding under Chapter 15 (see *In re Irish Bank Resolution Corp. Ltd.*, Case No. 13-12159).

possible, with the appropriate foreign financial authorities regarding the orderly liquidation of any covered financial company that has assets or operations in a country other than the U.S. In this manner, it could conceivably support a foreign resolution. However, given that the DFA does not apply to domestic branches of foreign banks or insurance companies, the scope of support that could be provided is limited. In addition, any support that could be offered is limited by the objectives of the Title II, which only refer to financial stability in the U.S. and do not take into consideration financial stability in the host jurisdictions. Lastly, any possibility to support a foreign resolution is subject to the initiation of a Title II proceeding, with the FDIC being appointed as a receiver for the covered financial company.

Banking. FDI Act does not provide for mechanisms or processes through which actions by a foreign resolution authority can be given prompt legal effect, either by way of recognition or by taking supportive measures.

U.S. branches. As noted above it may be conceivable that a foreign resolution proceeding of a foreign bank with U.S. branches may be recognized by the courts, under the U.S. comity principle. However, the standards of such principles are not clearly defined.

The extent to which the OCC or the receiver appointed by it (in case of a federal licensed uninsured branch) or the state authorities (in case of a state-licensed uninsured branch) would take supportive measures of actions taken by foreign resolution authorities would be subject to a case-by-case analysis, depending on the relevant circumstances. Federal or state authorities have a statutory responsibility to protect the interests of the creditors of the U.S. uninsured branches, as provided under the liquidation and ring-fencing regime described in EC 7.1. They would likely take action aimed at preserving the assets of the U.S. uninsured branches to the primary satisfaction of such creditors, particularly if the recoveries of the creditors of the uninsured branches would be lower in the absence of a ring-fence. This may be prejudicial to a cooperative solution and not consistent with the concept of providing support. It is also unlikely that a U.S. court will override any determination made by the local authorities (e.g., the OCC or the Superintendent) to initiate a liquidation or ring-fencing proceeding.

State Insurance. While their scope and content vary widely, the insurance resolution laws of many states provide some mechanisms through which the resolution authorities could, in principle, give effect to foreign resolution measures. For example, where a foreign insurer has assets in a state in which it is not domiciled and no receiver/liquidator has been appointed in the domiciliary jurisdiction, many insurance receivership laws (e.g., those based on the 1977 Insurers Supervision, Rehabilitation and Liquidation Model Act) empower the state commissioner to apply to court for orders to conserve the property or to liquidate the assets of the insurer. In either case, the court is given broad discretion to order whatever action it considers appropriate. While such action could include the support of foreign resolution measures, this would not necessarily be the case and would depend on what action was considered to be “appropriate.” As noted above, however, the liquidation of a foreign branch under state insurance law will be treated as a separate legal entity and its assets used to satisfy the claims for the branch’s creditors.

Findings. In the case of banks, there is no general statutory mechanism in the U.S. framework to give prompt legal effect in the U.S. legal framework to actions taken by a foreign resolution authority, either by way of recognition or by taking supportive measures. There may be circumstances where a foreign resolution proceeding may be recognized in the U.S., either under Chapter 15 or pursuant to the general principle of comity, which is well-established in U.S. courts. However, the current framework is fragmented. Moreover, in case of uninsured branches, whether a recognition would be granted depends on the action taken by the resolution authority responsible for the federal or state branch, and recognition would be unlikely if these

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| | <p>authorities initiate a liquidation or ring-fencing process.</p> <p>It is recommended therefore that the U.S. regime be examined holistically and be strengthened to establish clear and transparent mechanisms or processes through which actions by a foreign resolution authority can be given prompt legal effect in the U.S. resolution regime.</p> |
| EC7.3 | Recognition or support of foreign measures is provisional on equitable treatment in the foreign resolution proceeding of creditors of the firm in resolution that are located in the jurisdiction under review. |
| Description and findings re EC7.3 | <p>Chapter 15 of the Bankruptcy Code. Courts may refuse to take any action under Chapter 15, including recognizing a foreign proceeding, if the action would be “manifestly contrary to the public policy of the U.S.” When authorizing certain measures—such as entrusting the distribution of the debtor’s assets to the foreign representative or another person—the court must also be satisfied that the interests of creditors in the U.S. are sufficiently protected.</p> <p>Other applicable frameworks. No specific provisions exist with respect to ensuring the equitable treatment of local creditors as a condition to recognizing or supporting foreign resolution measures. This is consistent with the fact that there is limited scope for recognition or support either in state banking or insurance resolution frameworks. However, it can be expected that any action taken to give effect to foreign resolution measures would seek to ensure the equitable treatment of local creditors, given the resolution framework overall is designed to protect local stakeholders.</p> <p>Findings. Chapter 15 of the Bankruptcy Code—insofar as it applies as described above—contains certain safeguards aimed at protecting creditors in the U.S. Where Chapter 15 does not apply, given the limited scope for the recognition or support of foreign measures, there are no express provisions regarding the equitable treatment of creditors of a foreign bank or insurer that are located in the U.S. jurisdiction although such treatment can be inferred from the overall resolution framework.</p> |
| EC7.4 | The resolution regime enables the resolution authority to exercise resolution powers with respect to the local branch of a foreign firm to support a resolution carried out by a foreign home authority and on its own initiative where the home authority is not taking effective action or is acting in a manner that does not take sufficient account of the need to preserve financial stability in the local jurisdiction. |
| Description and findings re EC7.4 | <p>U.S. federal and state branches. As noted under EC 1.2 and EC 7.1, federal and state-licensed uninsured branches of foreign banks are subject to a specific, separate resolution regime.</p> <p>Under the IBA, upon revocation of the branch license or when other grounds are met—as noted under EC 7.1 above—the OCC may appoint a receiver, who shall take possession of the property and assets of the foreign bank in the U.S. and exercise the same rights, powers and authority exercised by receivers of national banks appointed by the OCC under the National Banking Act.¹⁹⁶ While the OCC appoints FDIC as a receiver for the resolution of national banks, in the case of federally licensed uninsured branches of foreign banks the law does not specify who it may appoint as a receiver. The scope of powers permitted under the National Banking Act is limited to the winding up of the business and the distribution of assets to creditors of uninsured branch.¹⁹⁷</p> |

¹⁹⁶ 12 US Code § 3102 (i) and (j).

¹⁹⁷ 12 US CODE § 197.

To the extent that the OCC appoints a receiver for the insured federal branches of foreign banking organization grandfathered by the Federal Deposit Insurance Corporation Improvement Act, the OCC must appoint the FDIC as receiver. The FDIC would conduct the receivership in accordance with the FDI Act.

State-licensed uninsured branches are subject to state law resolution regimes. In the case of NY, upon taking possession based on the grounds note under EC 7.1, the Superintendent shall liquidate or deal with such business and property in accordance with the liquidation regime, providing for the satisfaction of the creditors which had transactions with the NY uninsured branch on a priority basis. The court authorization is required to turn over proceeds from the liquidation to other offices of the foreign bank organization that are being liquidated in the U.S. Under different sets of provisions, the Superintendent (or any other person appointed by the Superintendent as a receiver or liquidator) may sell the property and assets of the uninsured branch without obtaining the approval of shareholders and any court. Nothing is said with respect to consents to the transfer which may be required under contract law, nor with respect to the regime for the transfer of liabilities.

The act of taking possession by the Superintendent may be stayed upon court challenge. A general provision allows the Superintendent “to make variations from the requirements of the Banking Law,” provided that such variations are in harmony with the spirit of the law, if “necessary because of the existence of unusual and extraordinary circumstances.” However, the precise scope of this provision remains unknown.

While counterparties to QFCs can exercise early termination rights and seize collateral in satisfaction of their claims, the NY Banking Law does not provide for a temporary stay from such early termination rights.

State Insurance. There would appear to be nothing at the state level that would require a state commissioner to initiate receivership proceedings with respect to a branch of a foreign insurer that is the subject of resolution proceedings abroad. Rather, the commencement of receivership proceedings is a matter of discretion for the state commissioner based on specified triggers that often include circumstances in which the insurer is subject to an application to appoint a receiver (trustee, custodian, conservator or sequestrator or similar fiduciary outside of the state) and “such appointment might oust the courts” of the relevant state “or might prejudice orderly delinquency proceedings” in the state.

The actions that a court may order with respect to the local branch of a foreign firm may not necessarily support resolution measures taken in the home jurisdiction. While resolution planning and the CMG framework may provide the opportunity for selected state commissioners to design appropriate resolution strategies for local branches in cooperation with their foreign counterparts, discussions on these issues is still at an early stage. Moreover, the liquidation of the branch would result in the ring-fencing of its assets to satisfy the claims of the branch’s creditors.

Findings. While the receiver appointed by the OCC and the state authorities may take discretionary action (or refrain from taking action) in a manner that supports the resolution carried out by a foreign home authority, it is unlikely that the relevant statutory provisions would lead to this outcome. The receiver appointed by the OCC has powers broadly focused on the winding up of the federal uninsured branch and the distribution of its assets. The powers of the Superintendent are broader in nature, but several uncertainties and conflicting provisions seem to come into play, such as with respect to the need to obtain creditors’ consent to any transfer authorized by the Superintendent. In both cases, the statutory duty to preserve the assets of the uninsured branch in the U.S., taking into account the requirement to satisfy on a priority basis the creditors which had transactions with the uninsured branch, may hinder efforts to support

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| | <p>action taken by foreign resolution authority, including when the branch may be systemic in the home country. It is therefore recommended that the U.S. resolution regime be amended to require the relevant U.S. authorities to cooperate with foreign and domestic resolution authorities in the context of a resolution of a foreign bank with a U.S. branch. (See also recommendations under KA 1).</p> <p>The regime governing the liquidation of foreign branches of insurance companies similarly provides for the ring-fencing of assets for the benefit of the branch's creditors. As is the case with the liquidation of a bank branch, consideration could be given to the amendment of the framework to provide greater flexibility to cooperate in a foreign resolution proceeding.</p> |
| EC7.5 | The resolution regime requires that, prior to exercising resolution powers in relation to a local subsidiary or branch of a foreign firm on its own initiative and independently of action taken by the home authority, the resolution authority give prior notice of the intended measures to and consult the home resolution authority of the firm. |
| Description and findings re EC7.5 | <p>DFA. No specific requirement exists as to the prior notification to, or consultation with, a home resolution authority of a foreign firm when resolution action is taken by U.S. authorities on their own initiative. The U.S. authorities have been negotiating the terms of cooperation agreements, providing that home authorities would be alerted when it becomes apparent that a domestic branch or incorporated entity is likely to enter resolution (see also KA 8 and 9). However, given their non-binding features, these agreements do not align the U.S. resolution regime to the requirements of EC 7.5.</p> <p>Banking. Same finding made above.</p> <p>U.S. Federal and State Branches. Same finding made above.</p> <p>State Insurance. While the initiation of receivership proceedings with respect to a foreign insurer or the local branch of a foreign insurer typically requires that the insurer be given notice and the right to a hearing, state resolution laws would generally not appear to provide for prior notice to be given to the relevant foreign resolution authority. While the framework of supervisory colleges, CMGs and cooperation agreements (COAGs) may provide the opportunity to put in place policies for the provision of prior notice to select foreign resolution authorities, no such policies are, as of yet, in place.</p> <p>Findings. With respect to banks and insurance companies, the U.S. resolution regime does not provide for a requirement to notify or to consult with the home resolution authority of a foreign firm prior to exercising resolution powers in relation to a local subsidiary or branch of such firm. It is recommended that such requirement be included in the U.S. resolution regime.</p> |
| EC7.6 | The resolution regime does not discriminate between creditors of the same class on the basis of their nationality, the location of their claim or the jurisdiction where their claim is payable. |
| Description and findings re EC7.6 | <p>DFA. No provision of the DFA discriminates between creditors on the basis of their nationality, location of their claim or jurisdiction where their claim is payable.</p> <p>Banking. Under the FDI Act, creditors are not discriminated against based on their nationality. However, the location and jurisdiction in which a depositor claim is payable may have an impact on the hierarchy of creditor claims applicable upon resolution of an IDI.</p> <p>Indeed, deposit liabilities are reimbursed by the receiver of a failed IDI before any general or senior liability of that institution.¹⁹⁸ While this depositor preference rule includes claims of both</p> |

¹⁹⁸ FDI Act 12 USC. § 1821 (d) 11.

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| | <p>insured deposits and uninsured deposits (with the FDIC enjoying the same status as the subrogee of the former category), the term “deposit liabilities” is not statutorily defined. In a recent rule-making modifying the regulations on deposit insurance, the FDIC has stated, in line with a 1994 advisory opinion by the then Acting General Counsel, that the term “deposit liability”, as used for the purposes of the depositor preference regime, includes a foreign branch deposit only if it is a “dually payable deposit”, i.e. payable at both the foreign branch and at a U.S. office of the failed IDI.¹⁹⁹ Therefore, deposits that are dually payable will be treated as a deposit liability (albeit an uninsured deposit), enjoying the depositor preference rule. Conversely, deposits that are payable only at the foreign branch do not enjoy any priority status and would be treated as unsecured liabilities, below deposit liabilities.</p> <p>The treatment, under the hierarchy of creditor claims, of a deposit held in a foreign branch of a U.S. chartered bank will therefore depend on the terms provided under the relevant deposit agreement between the depositor and such bank.</p> <p>State Insurance. State resolution laws do not discriminate between creditors of the same class on the basis of their nationality, the location of their claim or the jurisdiction where their claim is payable. The priorities for payment set out in the NAIC’s various model laws and in most state receivership laws do not provide for differential treatment on the basis of any of these criteria.</p> <p>Findings. Making foreign branch deposits subject to the U.S. deposit preference rule depending on where they are payable contradicts EC 7.6, which mentions the location where a claim is payable as one of the possible grounds of discrimination. Foreign branch deposits should rank in the same order as other depositors as they belong to the same class of creditors; however, they have a lower ranking if their claims are not payable in the U.S.</p> <p>The subordination of non-dually payable foreign branch deposits to the claims of home country depositors may also hinder the effectiveness of cross-border resolution, as the unequal treatment of such deposits could make it more problematic for third countries to recognize or enforce U.S. resolution proceedings. This concern can be mitigated, in practice, if banks switch to dually payable deposits. However, the discrimination would persist for those deposits that are not, for whatever reason, not converted into dually payable. It is therefore recommended that the U.S. regime be amended to subject foreign branch deposits to the depositor preference rule, whether or not they are dually payable in the U.S.</p> <p>No discrimination between creditors arises under the state insurance resolution laws.</p> |
| Assessment of KA7 | |
| Comments | <p>While, in certain circumstances, foreign resolution measures may be recognized under Chapter 15 of the Bankruptcy Code or by a court under the general principle of comity, the U.S. lacks an explicit statutory provision to give prompt effect to foreign resolution measures, either by way of recognition or by supporting action taken by a foreign resolution authority with respect to banks. Although the DFA requires the FDIC as a receiver to coordinate, to the maximum extent possible, with the appropriate foreign resolution authority in connection with a resolution under Title II, this cooperation mechanism could</p> |

¹⁹⁹ The rule was issued with the main purpose of clarifying the treatment of deposits in foreign branches of US chartered IDIs under the deposit insurance regulations. By modifying 12 C.F.R. § 330.3 (e), the FDIC has indeed clarified that such deposits are not FDIC-insured deposits, even when they are payable at an office within the United States. The clarification on the treatment of foreign branch deposits for the purposes of the deposit preference rule was not made in the final rule itself, but rather in the explanatory text accompanying the revised regulations on deposit insurance. See Federal Register, 78 F. R. 56583 (September 13, 2013).

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| | be clarified and broadened and a similar mechanism could be added to the FDI Act There is no requirement in place to notify and consult with the home resolution authority prior to exercising resolution powers in the U.S. The liquidation regime of U.S. branches of foreign institutions may undermine cross-border cooperation. The U.S. depositor preference rule is not in line with the requirements of EC 7.6, as it discriminates depending on whether the deposit is payable or not in the U.S. |
| 8. Crisis Management Groups | |
| KA 8.1 | Home and key host authorities of all G-SIFIs should maintain CMGs with the objective of enhancing preparedness for, and facilitating the management and resolution of, a cross-border financial crisis affecting the firm. CMGs should include the supervisory authorities, central banks, resolution authorities, finance ministries and the public authorities responsible for guarantee schemes of jurisdictions that are home or host to entities of the group that are material to its resolution, and should cooperate closely with authorities in other jurisdictions where firms have a systemic presence. |
| Essential criteria | |
| EC8.1 | If the jurisdiction under review is home jurisdiction of one or more G-SIFIs, a CMG is established and maintained for each such G-SIFI which includes the authorities with a role in resolution of the G-SIFI and a policy, process and criteria are maintained for determining which jurisdictions are host to entities that are material for a group-wide resolution of the firm and should be represented in the CMG. |
| Description and findings re EC8.1 | <p>DFA. In line with the policy framework for addressing the systemic and moral hazard risks associated with systemically important financial institutions—as developed under the oversight of the FSB and endorsed by G20 Leaders in November 2010—the U.S. authorities have established CMGs for the eight U.S. institutions that have been identified as G-SIBs, i.e. JP Morgan Chase, Citibank, Bank of America, Goldman Sachs, Morgan Stanley, Bank of New York Mellon, State Street and Wells Fargo.²⁰⁰</p> <p>Membership of the U.S.-based G-SIB CMGs includes the FDIC; the FRB and relevant Federal Reserve Bank; the OCC (for G-SIBs that have significant nationally chartered banks); and the SEC (for G-SIBs with large broker-dealer activity)—the U.S. Treasury, however, is not represented, despite its role in the “three keys” process and the reference in KA 8.1 to finance ministries. Host authorities that participate in the CMGs include supervisory authorities, central banks, resolution authorities, and deposit guarantee schemes from jurisdictions in which U.S. G-SIBs have significant activities or assets. CMG membership is reviewed annually by the FRB, in consultation with the FDIC. Membership criteria are not explicitly defined but in practice membership is based on the relative importance of the local activities for the firm as a whole (e.g. in terms of assets and revenues).</p> <p>In addition to the CMGs for the afore-mentioned G-SIBs, the authorities have established CMGs for two G-SIIs, i.e. American International Group and Prudential Financial. For both firms, the FSOC determined that material financial distress these firms could pose a threat to U.S. financial stability and hence, that both firms should be subject to supervision by the FRB and enhanced prudential standards.²⁰¹ CMG membership comprises the FIO, the Federal Reserve System, the</p> |

²⁰⁰ The 2014 update of the list of G-SIBs can be found here, <http://www.financialstabilityboard.org/2014/11/2014-update-of-list-of-global-systemically-important-banks/>. It should be noted that the CMG for Wells Fargo solely comprises US authorities, in view of the limited cross-border activities of the bank.

²⁰¹ DFA Section 113.

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| | <p>FDIC, relevant state insurance commissioners and international insurance regulators, foreign supervisors and resolution authorities. The central membership criterion is the materiality of the firm in the state or foreign country.</p> <p>The FSOC has also determined that, due to the systemic implications of a potential failure, MetLife shall be subject to supervision by the FRB. MetLife brought an action pursuant to DFA section 113 (h) in the U.S. District Court for the District of Columbia for the rescindment of this final determination in January 2015. The outcome of the law suit is pending. In view of the pending procedure, the establishment of a CMG for MetLife is expected to be initiated at the earliest in 2016.</p> <p>Banking. The FDI Act does not include specific statutory provisions that relate to CMGs.</p> <p>State Insurance. There are no specific statutory provisions in state law regarding CMGs of insurance companies.</p> <p>Findings. The establishment of CMGs has provided the U.S. authorities with important fora for elucidating aspects of the U.S. resolution regime under DFA and relevant host regimes. For the G-SIBs, CMGs have allowed the agencies to disseminate firms' recovery strategies; discuss cross-border resolution issues (e.g. legal rights, duties and obligations under the local laws of host jurisdictions, actions that can be taken by host authorities to facilitate continued access to financial market infrastructures); and to discuss DFA Title II resolution strategies (with the latter gravitating around the FDIC's SPE strategy) and steps to improve resolvability (as guided by the FDIC's firm-specific resolvability assessments). Moreover, recent CMGs included preliminary discussions on the nature, amount and distribution of gone-concern loss absorbing capacity that may be required in a Title II resolution to recapitalize the relevant firms. For the G-SIIs, whose CMGs were only established in 2014, discussion topics included the recovery and resolution planning process, cooperation matters and matters pertaining to information sharing.</p> |
| EC8.3 | <p>If the jurisdiction under review is the home jurisdiction of one or more G-SIFIs, it has processes to ascertain which jurisdictions that are not represented in the CMG assess the local operations of the G-SIFI as systemically important to the local financial system. There is a documented process for cooperation, or other evidence of efforts to cooperate with relevant authorities in those jurisdictions that have been identified through this process.</p> |
| Description and findings re EC8.3 | <p>DFA. While there is no formalized process in place to assess the systemic presence of G-SIFIs' operations in non-CMG host jurisdictions, foreign operations of U.S.-based G-SIBs are reviewed as part of the FBAs approach to enterprise-wide supervision. The FBAs have established robust processes for maintaining a comprehensive understanding of firms' structures, their material activities, corporate governance arrangements and risk management programs—both within the U.S. and abroad.²⁰²</p> <p>Moreover, the agencies have taken a variety of steps to facilitate cross-border cooperation with host supervisors, including via establishment of colleges of supervisors that, generally speaking, have a broader range of participants than CMGs. The FBAs share information bilaterally with home and host supervisors, either on the basis of formal arrangements (such as memoranda of understanding) or in response to ad hoc requests. The legal framework allows the FBAs to share relevant supervisory information with foreign banking supervisors, even in the absence of formal arrangements (e.g. memoranda of understanding), provided that the recipient itself is subject to</p> |

²⁰² See the detailed assessment of observance of the Basel Core Principles for Effective Banking Supervision for further details on the FBAs approach to consolidated supervision (link will be added).

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| | <p>confidentiality requirements (also see KA12).</p> <p>In the case of G-SIIs, there is also no formalized process in place to assess the systemic presence of G-SII operations in non-CMG host jurisdictions. The domiciliary state insurance commissioners have established colleges of supervisors for all insurance groups that meet the International Association of Insurance Supervisors' definition of an internationally active insurance group (IAIG), including for the FSOC-designated U.S.-based G-SIIs.</p> <p>Prior to the establishment of CMGs, supervisory colleges—organized in coordination with NAIC—have been used as a forum for preliminary discussions on crisis preparedness and crisis management arrangements.</p> <p>While there is limited experience with the functioning of the CMGs for the two G-SIIs, the inaugural meetings that took place in Q4-2014 were considered helpful to foster a dialogue on issues pertaining to recovery and resolution planning. Discussion topics included various aspects related to the recovery and resolution planning process, frameworks for cross-border cooperation and participants' legal authority to share relevant information. From the U.S. perspective, state and federal authorities involved in the supervision of insurance firms have adequate powers to share information with foreign supervisory authorities in order to coordinate preparations for a crisis management and coordination.</p> <p>Banking. The FDI Act does not include specific statutory provisions that relate to CMGs.</p> <p>State Insurance. There are no specific statutory provisions in state law regarding the cooperation with non-CMG members.</p> <p>Findings. There is no formalized process in place to assess the systemic presence of G-SIFIs' operations in non-CMG host jurisdictions. The CMGs operate in parallel to the supervisory colleges for the U.S.-based G-SIBs and G-SII (with the latter having been identified as IAIGs). The supervisory colleges comprise more members than the CMGs and can help facilitate the coordination with non-CMG members. Going forward, the U.S. authorities should endeavor to align current practices for cooperation with non-CMG host authorities with the draft guideline for cooperation and information-sharing with host authorities from jurisdictions that are not represented on CMGs,²⁰³ published by the FSB in October 2014.</p> |
| <p>EC8.4</p> | <p>The jurisdiction under review (if it is not itself the home jurisdiction) participates in the CMG for one or more G-SIFIs when invited.</p> |
| <p>Description and findings re EC8.4</p> | <p>DFA. The FBAs, together with the relevant state supervisors, participate in CMGs for non-U.S. G-SIBs. Inter alia, this relates to CMGs for G-SIBs from France, Germany, Japan, Spain, Switzerland and the United Kingdom. On behalf of the U.S. authorities, participants include the FDIC; the Federal Reserve System; the OCC and relevant state supervisors. Relevant state insurance commissioners²⁰⁴ and international insurance regulators also participate in CMGs for foreign G-SIIs.</p> <p>The U.S. authorities have not declined any invitations to participate in CMGs of foreign G-SIBs and G-SIIs.</p> |

²⁰³ http://www.financialstabilityboard.org/wp-content/uploads/c_141017.pdf.

²⁰⁴ I.e. the state insurance commissioners of California and Minnesota for the CMG for Germany-based Allianz; the commissioner of New York in the CMG for France-based AXA; and the commissioner of Michigan in the CMG for UK-based Prudential.

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| | <p>Banking. The FDI Act does not include specific statutory provisions that relate to CMGs</p> <p>State Insurance. There are no specific statutory provisions in state law regarding the participation in CMGs for foreign insurance companies.</p> <p>Findings. The U.S. federal and state authorities participate in foreign CMGs when invited.</p> |
| Assessment of KA8 | |
| Comments | The establishment of CMGs for the U.S.-based G-SIBs and two of the three G-SIIs (a CMG for MetLife has not yet been established), in line with international commitments, has provided the U.S. authorities with important fora for enhancing the preparedness for, and facilitating the management and resolution of, cross-border distress. The U.S. Treasury, however, is not represented, despite its role in the “three keys” process and the reference in KA 8.1 to finance ministries. Existing modalities for cross-border coordination could be further strengthened via the development of explicit CMG membership criteria, together with arrangements for cooperation and information-sharing with host authorities that are not represented on CMGs—with the latter including the development of consistent criteria for assessing the systemic presence of local operations in non-CMG host jurisdictions. |
| 9. Institution-specific Cross-border Cooperation Agreements | |
| KA9.1 | <p>For all G-SIFIs, at a minimum, institution-specific cooperation agreements, containing the essential elements set out in Annex I, should be in place between the home and relevant host authorities that need to be involved in the planning and crisis resolution stages. These agreements should, inter alia:</p> <ul style="list-style-type: none"> (i) establish the objectives and processes for cooperation through CMGs; (ii) define the roles and responsibilities of the authorities pre-crisis (that is, in the recovery and resolution planning phases) and during a crisis; (iii) set out the process for information sharing before and during a crisis, including sharing with any host authorities that are not represented in the CMG, with clear reference to the legal bases for information sharing in the respective national laws and to the arrangements that protect the confidentiality of the shared information; (iv) set out the processes for coordination in the development of the RRP for the firm, including parent or holding company and significant subsidiaries, branches and affiliates that are within the scope of the agreement, and for engagement with the firm as part of this process; (v) set out the processes for coordination among home and host authorities in the conduct of resolvability assessments; (vi) include agreed procedures for the home authority to inform and consult host authorities in a timely manner when there are material adverse developments affecting the firm and before taking any significant action or crisis measures; (vii) include agreed procedures for the host authority to inform and consult the home authority in a timely manner when there are material adverse developments affecting the firm and before taking any discretionary action or crisis measure; (viii) provide an appropriate level of detail with regard to the cross-border implementation of specific resolution measures, including with respect to the use of bridge institution and bail-in powers; (ix) provide for meetings to be held at least annually, involving top officials of the home and relevant host authorities, to review the robustness of the overall resolution strategy for G-SIFIs; and (x) provide for regular (at least annual) reviews by appropriate senior officials of the operational plans implementing the resolution strategies. |

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| <p>KA9.2</p> | <p>The existence of agreements should be made public. The home authorities may publish the broad structure of the agreements, if agreed by the authorities that are party to the agreement.</p> |
| <p>Essential criteria</p> | |
| <p>EC9.1</p> | <p>If the jurisdiction under review is home to a G-SIFI it maintains institution-specific cross-border cooperation agreements (COAGs) with all members of the CMG in the form of either a multilateral agreement, bilateral agreements, or a combination of multilateral and bilateral agreements and publicly discloses the existence of those agreements.</p> |
| <p>Description and findings re EC9.1</p> | <p>DFA. U.S. home authorities have executed COAGs with 21 authorities from 11 jurisdictions for all seven U.S. G-SIBs with significant cross-border operations. The COAG template, reviewed by the mission, covers the following aspects.</p> <ul style="list-style-type: none"> ▪ Objectives, with the agreements setting out the parties’ intentions regarding cross-border cooperation and information exchange, without creating binding obligations on the signatories. ▪ General framework for cooperation, covering the roles, responsibilities and powers of the signatories in normal times and during crises episodes ▪ Home and host commitments, including the development of the group-wide resolution plan, the coordination of firm-specific resolvability assessments and the commitment to take into account the overall effect of actions on financial stability in other jurisdictions (home authority); and alerting the home authority without undue delay if local operations encounter material difficulties or if it becomes apparent that said operations are likely to enter the host authority’s resolution regime (host authorities). ▪ Cooperation mechanisms and information sharing framework, covering meeting frequency, information to be exchanged and confidentiality arrangements. ▪ Cross-border implementation of resolution measures, including the intention to work together to address potential impediments to cross-border implementation of resolution actions. <p>The preparation of multilateral COAGs for the U.S.-based G-SIIs remains ongoing. The U.S. authorities have initiated discussions with relevant foreign authorities but agreements are not expected to be finalized before the parties involved have coalesced on credible resolution strategies.</p> <p>The agencies have not taken any decisions on disclosure of the agreements.</p> <p>Banking. The FDI Act does not include specific statutory provisions that relate to COAGs.</p> <p>State Insurance. There are no specific statutory provisions in state law regarding COAGs.</p> <p>Findings. COAGs for the U.S.-based G-SIIs have not yet been finalized.</p> |
| <p>EC9.3</p> | <p>If the jurisdiction under review is invited by the home jurisdiction to be party to a COAG for a G-SIFI it has concluded or is engaging in good faith negotiations towards the conclusion of an agreement with other members of the CMG.</p> |
| <p>Description and findings re EC9.3</p> | <p>DFA. At the time of the mission, multilateral COAGs for both the G-SIB and G-SII CMGs in which the U.S. authorities participate as host authority had not been finalized. The authorities, however, are engaging in good faith negotiations towards the conclusion of the agreements.</p> |

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| | <p>Banking. The FDI Act does not include specific statutory provisions that relate to COAGs.</p> <p>State Insurance. There are no specific statutory provisions in state law regarding COAGs.</p> <p>Findings. COAGs for foreign G-SIBs and G-SIIs have not yet been finalized.</p> |
| Assessment of KA9 | |
| Comments | Pursuant to the obligation for the FDIC—in its capacity as receiver for covered financial companies under DFA’s Title II—to coordinate, to the maximum extent possible, with relevant foreign authorities on the orderly liquidation of a covered financial company that has assets or operations outside the U.S., ²⁰⁵ the agencies have initiated extensive dialogues with relevant host authorities about aspects pertaining to resolution and resolution planning. U.S. home authorities have executed COAGs with 21 authorities from 11 jurisdictions for all seven U.S. G-SIBs with significant cross-border operations. The finalization of COAGs creates a firm anchor for future cooperation. |
| 10. Resolvability Assessments | |
| KA10.1 | Resolution authorities should regularly undertake, at least for G-SIFIs, resolvability assessments that evaluate the feasibility of resolution strategies and their credibility in light of the likely impact of the firm’s failure on the financial system and the overall economy. Those assessments should be conducted in accordance with the guidance set out in Annex II. |
| KA10.2 | In undertaking resolvability assessments, resolution authorities should in coordination with other relevant authorities assess, in particular: <ul style="list-style-type: none"> (i) the extent to which critical financial services, and payment, clearing and settlement functions can continue to be performed; (ii) the nature and extent of intra-group exposures and their impact on resolution if they need to be unwound; (iii) the capacity of the firm to deliver sufficiently detailed accurate and timely information to support resolution; and (iv) the robustness of cross-border cooperation and information sharing arrangements. |
| KA10.3 | Group resolvability assessments should be conducted by the home authority of the G-SIFI and coordinated within the firm’s CMG taking into account national assessments by host authorities. |
| KA10.4 | Host resolution authorities that conduct resolvability assessments of subsidiaries located in their jurisdiction should coordinate as far as possible with the home authority that conducts resolvability assessment for the group as a whole. |
| KA10.5 | To improve a firm’s resolvability, supervisory authorities or resolution authorities should have powers to require, where necessary, the adoption of appropriate measures, such as changes to a firm’s business practices, structure or organisation, to reduce the complexity and costliness of resolution, duly taking into account the effect on the soundness and stability of on-going business. To enable the continued operations of systemically important functions, authorities should evaluate whether to require that these functions be segregated in legally and operationally independent entities that are shielded from group problems. |
| Essential criteria | |
| EC10.1 | If the jurisdiction under review is home to one or more G-SIFIs, or domestically incorporated |

²⁰⁵ DFA Section 210 (a) (1) (N).

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| | firms that are subject to a requirement for resolution plans, arrangements and processes are in place whereby the resolution authorities undertake, in cooperation with members of the firm's CMG group resolvability assessments regularly, including when there are material changes to the firm's business or structure. |
| Description and findings re EC10.1 | <p>DFA. The FDIC has undertaken initial assessments of the feasibility and credibility of the resolution strategies prepared under DFA Title II for the U.S.-based G-SIBs with significant cross-border operations. In accordance with FSB requirements, the assessments comprise the following aspects</p> <ul style="list-style-type: none"> (i) the identification of resolution strategies that would be <i>feasible</i>, in view of resolution tools available, the firm's recovery and resolution plan; and the authorities' capacity to apply the tools at short notice and other domestically incorporated banks that are subject to resolution planning requirements; (ii) the <i>credibility</i> of all resolution strategies deemed feasible, in view of the likely impact of the firm's failure on global and national financial systems and real economies; and (iii) the determination of actions that may be necessary to improve resolvability, possibly including changes to the firm's recovery and resolution plan, or its structure or operations. <p>The results of the FDIC's preliminary assessments have been discussed in the CMGs of U.S.-based G-SIBs, with the aim to deepen the analysis of potential impediments to orderly resolution of the firms (also see EC 8.1).</p> <p>Documentation provided to the mission indicates that the breadth and contents of the FDIC's approach to resolvability assessments is aligned with the FSB's detailed guidance thereon.²⁰⁶ In particular, the assessments cover aspects pertaining to (a) firms' structure and operations, (b) intragroup exposures, (c) continuity in FMI membership, (d) management information systems, and (e) coordination of national resolution regimes and tools (together amounting to an assessment of the feasibility of resolution strategies); together with an analysis of impact of a firm's failure on financial markets, FMI, funding conditions, capital and the broader economy. Where practicable, the analyses are informed by the modalities of the SPE strategy, including the expectation that operating subsidiaries will remain intact and that the continuity of critical functions can be ensured.</p> <p>At the time of the mission, the FDIC had not yet finalized similar assessments for smaller BHCs that are subject to resolution planning requirements. Similarly, the agencies had not completed group resolvability assessments for NBFC that are deemed to be systemically important.</p> <p>Banking. All of the U.S. based G-SIBs that have IDIs are required to submit resolution plans under the FDI Act. The assessment of the resolvability of such firms is ongoing as part of the group-wide resolution plans that are discussed at the level of the CMGs. The FDIC participates in the discussions, as highlighted above.</p> <p>State Insurance. The state commissioners were not involved in the preparation of resolvability assessments, but have been consulted as part of the agencies' review of the living wills of relevant firms.</p> <p>Findings. The preparation of group resolvability assessments for G-SIBs is in train, with initial</p> |

²⁰⁶ See Appendix I-Annex 3 of the KA.

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| | assessments having been discussed in the banking groups' CMGs. Similar assessments are not yet in train for designated NBFCs, and are not envisaged for other domestically incorporated firms, including other BHCs subject to Title I resolution planning requirements . |
| EC10.2 | If the jurisdiction under review is host to one or more G-SIFIs, or domestically incorporated firms that are subject to a requirement for resolution plans, it has in place arrangements and processes whereby the resolution authorities cooperate with the home jurisdiction and contribute to the development of the resolvability assessments were invited to do so by the home jurisdiction, including by sharing results of local resolvability assessments with the home authority. |
| Description and findings re EC10.2 | <p>DFA. In line with FSB guidance, the preparation of resolvability assessments for G-SIFIs headquartered in countries other than the U.S. is the responsibility of the firm's home authority. The U.S. authorities contribute to the preparation of group resolvability assessments for non-U.S. based G-SIFIs to the extent that they are represented in the firm-specific CMGs (also see KA 8).</p> <p>Banking. A number of foreign-owned IDIs are required to submit resolution plans under the FDI Act, some of which belong to banking groups that have been designated as systemic at a global level (e.g., Deutsche, HSBC, Santander). The assessment of the resolvability of such firms is ongoing as part of the group-wide resolution plans that are discussed at the level of the CMGs that are chaired by the home authorities. The FDIC participates in the discussions.</p> <p>State Insurance. The preparation of resolvability assessments for foreign-owned G-SIFIs is, generally speaking, less advanced than for the G-SIBs. State commissioners, however, contribute to the extent that they participate in the CMGs of the relevant firms.</p> <p>Findings. The resolvability of U.S. operations of foreign G-SIFIs is being incorporated in the discussions of group-wide resolvability assessments in the CMGs.</p> |
| EC10.3 | The supervisory authorities or resolution authorities have the power to require changes to a firm's business practices, legal, operational or financial structures or organisation that are necessary to improve the resolvability of the firm. |
| Description and findings re EC10.3 | <p>DFA. The ability of resolution authorities to mandate changes to a firm's business practices, legal, operational or financial structures or organization—with a view to improve resolvability in situations where the firm itself fails to take measures to address identified impediments—is a cornerstone of effective frameworks for resolution planning. The U.S. FBAs have a number of statutory powers to require the adoption of measures that can help to reduce the complexity and costliness of resolution.</p> <p>Pursuant to Section 165(d) of the DFA, the FRB and FDIC are required to jointly review institutions' plans for orderly resolution under the U.S. Bankruptcy Code, as governed by DFA's Title I. Whenever they jointly determine that the plan is not credible or would not facilitate an orderly resolution of the company, they shall inform the company in writing of such determination. Failure to resubmit the plan with revisions that address the agencies' concerns within 90 days (subject to extensions granted by the agencies) may result in formal actions being taken against the company, which shall remain in force until the company resubmits a plan that remedies the deficiencies. Such actions may incline the imposition of more stringent capital, leverage, or liquidity requirements, or restrictions on the growth, activities, or operations of the company (or any subsidiary thereof).</p> <p>If the company fails to submit an acceptable plan within two years from the imposition of the</p> |

afore-mentioned measures, the agencies may order the company to divest certain assets or operations to facilitate an orderly resolution.²⁰⁷ Prior to issuing a notice of deficiencies, determining that additional requirements should be imposed or issuing a divestiture order that is likely to have a significant impact on a regulated subsidiary or IDI of the company, the FRB is required to consult with each FSOC member that is involved in the supervision thereof.²⁰⁸

In addition, the FRB is authorized to impose additional prudential standards on NBFCs and BHCs with consolidated assets greater than \$50 billion. Such standards could include the introduction of a contingent capital requirement; enhanced public disclosures; short-term debt limits; and any other prudential standards that the FRB may deem appropriate. Again, any requirement that is likely to have a significant impact on a regulated subsidiary or IDI of the company warrants prior consultation of each FSOC member that is involved in the supervision thereof.

In the joint press release on the findings of their review of the second iteration of the DFA Title I resolution plans for the largest firms (total consolidated assets > \$250 billion), the agencies indicated that they expect to use the afore-mentioned authority if the identified shortcomings are not addressed in the next iteration of the firms' submissions.

Banking. Neither the FDI Act, nor the IDI Rule provide specific powers to require changes to a firm's business practices, legal, operational or financial structures or organization that may be deemed necessary to improve the resolvability of the firm. However, the FBA has a wide range of supervisory options when an IDI is not complying with U.S. laws, regulations or supervisory orders, or is engaged in unsafe or unsound practices. Given that certain organizational or operational impediments to resolution may also be considered unsafe and unsound practices—for example the non-ability of covered IDI to ensure continuity of critical services and ensure timely and accurate reporting—the FDIC is of the view that the regular supervisory toolkit could be leveraged to improve IDIs' resolvability.

Pursuant to the FDIA and other acts, the FDIC and other FBAs have the authority to, among others, impose cease and desist orders, remove board members from office, impose monetary penalties on IDIs or their board members, facilitate mergers and take prompt corrective action against undercapitalized IDIs.

State Insurance. To a certain extent, the insurance commissioners have statutory power under state laws to require changes to a firm's business practices or structures or organization to improve its resolvability before entering into receivership. Although improving firms' resolvability is not necessarily the primary objective of the relevant legislation, the commissioners have certain broad group-wide supervisory powers to direct/prohibit actions in a company (i.e., required regulatory approvals) and additionally, commissioners are able to require insurance companies to take certain actions with regard to its operational or financial structure after placing it into special administrative supervision.

Traditionally, the main focus is on dialogue and informal influence on the insurance companies to adjust their business practices in case of indications for potential pending financial distress. After an insurance company has been put into receivership, the commissioner as receiver is permitted to make any changes to a firm's legal, operational or

²⁰⁷ DFA Section 165(d) (5) (B) (ii).

²⁰⁸ 12 CFR § 243.7.

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| | <p>financial structures or organization depending on prior court approval.</p> <p>Findings. The agencies have broad powers under the DFA to require changes to the business practices, legal, operational and financial structures, or organizations of designated NBCFs and BHCs that are subject to Title I resolution planning requirements, with the aim to address impediments to effective resolution. The FDI Act does not provide for specific powers to improve resolvability, but does provide for broad powers to correct, or otherwise address, any practice or condition that the FBAs consider to be unsafe and unsound. State law only provides for powers to make similar changes to insurance firms under certain supervisory powers and in the case of special administrative supervision when the relevant conditions have been met. .</p> |
| Assessment of KA10 | |
| Comments | <p>The authorities have made progress preparing resolvability assessments, focusing—understandably—on the U.S.-based G-SIBs, in view of the serious adverse effects that their failure could have on financial stability in the U.S. Going forward, efforts to prepare resolvability assessments should be broadened, with the aim to ensure that resolvability assessments are prepared for all institutions whose failure could have serious adverse effects on the U.S. financial system and overall economy.</p> <p>The preparation of resolvability assessments is particularly relevant for complex insurance groups that have been designated by the FSOC for FRB supervision to gauge the feasibility of an SPE resolution strategy under the OLA. Via the resolvability assessment, the authorities can effectively (a) enhance awareness of the implications of initiating resolution procedures against NBCFs under DFA Title II; (b) identify factors and conditions that may adversely affect the effective implementation of Title II resolution actions; and (c) help determine specific actions necessary to achieve greater resolvability.</p> <p>The agencies have broad powers under the DFA to require changes to the business practices, legal, operational and financial structures, or organizations of designated NBCFs and BHCs that are subject to Title I resolution planning requirements, with the aim to address impediments to effective resolution. The FDI Act does not provide for specific powers to improve resolvability. State law provides for powers to make similar changes to insurance firms through the exercise of certain supervisory powers and under administrative supervision.</p> |
| 11. Recovery and Resolution Planning | |
| KA11.1 | Jurisdictions should put in place an on-going process for recovery and resolution planning, covering at a minimum domestically incorporated firms that could be systemically significant or critical if they fail. |
| KA11.2 | Jurisdictions should require that robust and credible RRP, containing the essential elements of Recovery and Resolution Plans set out in Annex III, are in place for all G-SIFIs and for any other firm that its home authority assesses could have an impact on financial stability in the event of its failure. |
| KA11.3 | The RRP should be informed by resolvability assessments (see Key Attribute 10) and take account of the specific circumstances of the firm and reflect its nature, complexity, interconnectedness, level of substitutability and size. |
| KA11.4 | Jurisdictions should require that the firm’s senior management be responsible for providing the necessary input to the resolution authorities for (i) the assessment of the recovery plans; and (ii) the preparation by the resolution authority of resolution plans. |
| KA11.5 | Supervisory and resolution authorities should ensure that the firms for which a RRP is required maintain a recovery plan that identifies options to restore financial strength and viability when |

the firm comes under severe stress. Recovery plans should include:

- (i) credible options to cope with a range of scenarios including both idiosyncratic and market wide stress;
- (ii) scenarios that address capital shortfalls and liquidity pressures; and
- (iii) processes to ensure timely implementation of recovery options in a range of stress situations.

- KA11.6** The resolution plan is intended to facilitate the effective use of resolution powers to protect systemically important functions, with the aim of making the resolution of any firm feasible without severe disruption and without exposing taxpayers to loss. It should include a substantive resolution strategy agreed by top officials and an operational plan for its implementation and identify, in particular:
- (i) financial and economic functions for which continuity is critical;
 - (ii) suitable resolution options to preserve those functions or wind them down in an orderly manner;
 - (iii) data requirements on the firm's business operations, structures, and systemically important functions;
 - (iv) potential barriers to effective resolution and actions to mitigate those barriers;
 - (v) actions to protect insured depositors and insurance policy holders and ensure the rapid return of segregated client assets; and
 - (vi) clear options or principles for the exit from the resolution process.
- KA11.7** Firms should be required to ensure that key Service Level Agreements can be maintained in crisis situations and in resolution, and that the underlying contracts include provisions that prevent termination triggered by recovery or resolution events and facilitate transfer of the contract to a bridge institution or a third party acquirer.
- KA11.8** At least for G-SIFIs, the home resolution authority should lead the development of the group resolution plan in coordination with all members of the firm's CMG. Host authorities that are involved in the CMG or are the authorities of jurisdictions where the firm has a systemic presence should be given access to RRP and the information and measures that would have an impact on their jurisdiction.
- KA11.9** Host resolution authorities may maintain their own resolution plans for the firm's operations in their jurisdictions cooperating with the home authority to ensure that the plan is as consistent as possible with the group plan.
- KA11.10** Supervisory and resolution authorities should ensure that RRP are updated regularly, at least annually or when there are material changes to a firm's business or structure, and subject to regular reviews within the firm's CMG.
- KA11.11** The substantive resolution strategy for each G-SIFI should be subject, at least annually, to a review by top officials of home and relevant host authorities and, where appropriate, the review should involve the firm's CEO. The operational plans for implementing each resolution strategy should be, at least annually, reviewed by appropriate senior officials of the home and relevant host authorities.
- KA11.2** If resolution authorities are not satisfied with a firm's RRP, the authorities should require appropriate measures to address the deficiencies. Relevant home and host authorities should provide for prior consultation on the actions contemplated.

| Essential criteria | |
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| EC11.1 | The resolution regime requires the development and maintenance of RRP for all G-SIFIs for which the jurisdiction is the home country, and any other firm that could have an impact on financial stability in the event of its failure. |
| Description and findings re EC11.1 | <p>DFA. Pursuant to Section 165(d) of the DFA, all NBFCs supervised by the FRB and BHCs with consolidated assets equal or greater than \$50 billion are required to submit plans (“living wills”) supporting rapid and orderly resolution of the firm under the U.S. Bankruptcy Code in the event of material distress or failure, with such living wills including, at minimum</p> <ul style="list-style-type: none"> (i) information regarding the manner and extent to which any IDI affiliated with the company is adequately protected from risks arising from the activities of any nonbank subsidiaries of the company; (ii) full descriptions of the ownership structure, assets, liabilities, and contractual obligations of the company; (iii) an identification of the cross-guarantees tied to different securities, identification of major counterparties, and a process for determining to whom the collateral of the company is pledged; and (iv) any other information that the FRB and FDIC jointly require by rule or order. <p>Following the adopting of the DFA, the FRB and FDIC have released a number of documents that provide further guidance on firms’ Title I living wills. These documents are discussed in more detail in EC11.5.</p> <p>The implementing Rule of the provisions of section 165(d) (hereinafter 165(d) Rule) prescribes staggered submissions, with the sequencing being based on asset size of the covered companies. As a result, the largest companies (total nonbank assets of at least \$250 billion) were required to submit their first living wills on July 1, 2012; companies with total nonbank assets of at least \$100 billion but below \$250 billion were required to submit their plans by July 1, 2013; with other covered companies were mandated to submit by December 31, 2013. The two U.S. based G-SIFIs that were designated by the FSOC for FRB supervision were required to submit their first living wills by July 1, 2014.</p> <p>As a backup to the bankruptcy based resolution process envisaged in Title I, the DFA’s Title II OLA provides the FDIC with the ability to resolve systemically important financial institutions, to be utilized when bankruptcy or ordinary insolvency procedures could have serious adverse effects on financial stability in the U.S. Although the DFA does not specify how a Title II resolution should be structured, it does establish important policy goals. First, to minimize moral hazard and promote market discipline, the FDIC is expected to resolve the covered financial company in a manner that protects U.S. taxpayers by allocating losses to creditors and shareholders.²⁰⁹ Second, management shall be held accountable for the company’s failure and, hence, will not be retained following the resolution.²¹⁰ Third, the FDIC is required to coordinate, to the maximum extent possible, with the appropriate foreign authorities regarding the orderly resolution of covered financial companies that have assets or operations outside the U.S.²¹¹ The FDIC’s resolution plans under DFA’s Title II are not bound by the firms’ submissions under Title I,</p> |

²⁰⁹ DFA Section 204 (a).

²¹⁰ *Ibid.*

²¹¹ DFA Section 210(a)(1)(N).

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| <p>but can usefully be informed by the detailed information provided therein.</p> <p>In December 2013, the FDIC published a notice on the SPE strategy, developed to enable the FDIC to place systemically important institutions in a receivership process in situations where a looming default cannot be prevented via private sector solutions and resolution under the U.S. Bankruptcy Code (as per DFA's Title I) would be deemed to have serious adverse effects on financial stability. In essence, SPE is a recapitalization strategy that takes advantage of the holding company structure of U.S.-based banking groups by effecting the resolution at the level of the top-tier holding company and thus allowing the operating subsidiaries to remain "open".</p> <p>The applicability and feasibility of the SPE strategy for the two U.S.-based G-SIIs that have been designated for FRB supervision, and thus far within the remit of the OLA, is unclear. As insurance holding companies they are subject to state insurance holding company laws prescribing that the assets and liabilities of each operating entity are duly separated from each other and also from the firms' holding companies. There is no consolidation of assets for all entities within a group, which aims to insure better protection of the policyholders of the individual insurance companies. Any change in the ownership of the insurance companies, directly or indirectly, would be subject to state laws and thus require approval by the domiciliary state insurance commissioner.</p> <p>In August 2014, the FRB and FDIC noted that their review of the 2013 living wills of the eleven banking groups with assets of at least \$250 billion²¹² had highlighted several common shortcomings, including (a) assumptions that the agencies regard as unrealistic or inadequately supported, such as assumptions about the likely behavior of customers, counterparties, investors, central clearing facilities, and regulators; and (b) the failure to make, or even to identify, the kinds of changes in firm structure and practices that would be necessary to enhance the prospects for orderly resolution.²¹³</p> <p>The FBAs expect covered companies to demonstrate that they are making significant progress to address all the shortcomings identified by the agencies, and are taking steps to improve their resolvability under the U.S. Bankruptcy Code, including:</p> <ul style="list-style-type: none"> (i) establishing a rational and less complex legal structure that would take into account the best alignment of legal entities and business lines to improve the firm's resolvability; (ii) developing a holding company structure that supports resolvability; (iii) amending, on an industry-wide and firm-specific basis, financial contracts to provide for a stay of certain early termination rights of external counterparties triggered by insolvency proceedings; (iv) ensuring the continuity of shared services that support critical operations and core business lines throughout the resolution process; and (v) demonstrating operational capabilities for resolution preparedness, such as the ability to produce reliable information in a timely manner. <p>The agencies expect to use their authority under section 165(d) to determine that a Title I living</p> |
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²¹² Bank of America, Bank of New York Mellon, Barclays, Citigroup, Credit Suisse, Deutsche Bank, Goldman Sachs, JPMorgan Chase, Morgan Stanley, State Street Corp., and UBS.

²¹³ <http://www.federalreserve.gov/newsevents/press/bcreg/20140805a.htm>, and <https://www.fdic.gov/news/news/press/2014/pr14067.html>. Note that only the FDIC concluded that firms' 2013 submissions were "not credible and do not facilitate an orderly resolution under the Bankruptcy Code".

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| | <p>will does not meet the requirements of the DFA in the event that the relevant companies fail to address the identified shortcomings in their 2015 submission (due by July 1, 2015).</p> <p>The FRB and the FDIC did not yet give any feedback to the 2014 submissions of the two US based G-SIIs. The timeframe for submitting their 2015 living wills was extended to December 1, 2015 at the initiative of the FBAs.</p> <p>The requirement of recovery planning for large financial institutions—i.e. NBFCs designated for FRB supervision by the FSOC, large banking organizations (LBO) with consolidated assets of at least \$50 billion and large FBO with combined assets of U.S. operations of at least \$50 billion—was introduced by the FRB via a supervisory letter in December 2012. See EC 11.4 for details.</p> <p>Banking. In September 2011, in parallel with the 165(d) Rule, the FDIC issued a Rule requiring IDIs with \$50 billion or more in total assets to periodically submit to the FDIC a plan for the orderly resolution of such institutions in the event of failure.²¹⁴ This so-called IDI Rule establishes the requirements for submission and the contents of an IDI resolution plan, as well as procedures for review by the FDIC. In essence, the Rule requires covered IDIs to submit plans that would enable the FDIC, in its capacity as receiver, to resolve a failing IDI under Sections 11 and 13 of the FDIA,²¹⁵ in a manner that (a) ensures that depositors receive access to their insured deposits within one business day from the institution's failure; (b) maximizes the net present value return from the sale of dispositions of the failed IDI's assets; and (c) minimizes the amount of loss to be realized by the institution's creditors.</p> <p>The FDIC intends for the 165(d) Rule and IDI Rule to work in tandem, both from a procedural perspective and in the contents of the plans. In this context, the timing of resolution plans submissions under both Rules has been aligned.</p> <p>State Insurance. There are no statutory requirements for the development and maintenance of recovery and resolution plans under state laws.</p> <p>Findings. Pursuant to Title I of the DFA, FSOC designated NBFCs and BHCs with consolidated assets of at least \$50 billion are required to prepare living wills that can support their rapid and orderly resolution under U.S. bankruptcy law in the event of material distress or failure. Similar plans are required for IDIs with \$50 billion or more in assets, with the <i>caveat</i> that the latter focus more narrowly on the protection of insured depositors and the FDIC's DIF. In parallel, the FDIC has been developing resolution strategies under DFA Title II, focusing on U.S.-based G-SIBs. Where appropriate, the FDIC's Title II plans leverage information provided by the firms in their living wills. Recovery plans are to be prepared by FSOC designated NBFCs, LBOs with consolidated assets of at least \$50 billion and Large FBOs with combined assets of U.S. operations of at least \$50 billion.</p> |
| EC11.2 | The development and maintenance of RRP for firms covered by EC 11.1 that are not G-SIFIs takes into account the specific circumstances of individual firms, including their nature, complexity, interconnectedness, level of substitutability and size and the extent of cross-border operations and involves appropriate arrangements for cross-border cooperation. |
| Description and findings | DFA. To address any potential risks posed to financial stability, the DFA authorizes the FSOC to determine that a NBFC shall be supervised by the FRB and shall be subject to prudential standards. ²¹⁶ In making its determinations, the FSOC is required to consider, among others, |

²¹⁴ 12 CFR § 360.10.

²¹⁵ FDI Act 12 USC. § 1821 and 1823.

²¹⁶ DFA Section 113 (a)(1).

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| re EC11.2 | <p>leverage; off balance-sheet exposures; transactions and relationships of the company with other significant NBFCs and BHCs; the importance of the company as a source of credit; the nature, scope, size, scale, concentration, interconnectedness, and mix of its activities; its regulatory status; its asset size; the amount and composition of its liabilities; and any other risk-related factors that the FSOC deems appropriate.</p> <p>By exercising its statutory authority, the FSOC can effectively extend the application of Title I resolution planning requirements to any domestic NBFC that is deemed to be systemically significant or critical at the point of failure. For BHCs, DFA section 165(d) mandates the preparation of plans for the orderly resolution under the U.S. Bankruptcy code for companies with consolidated assets equal or greater than \$50 billion. The legal framework does not provide the agencies with any discretion to apply Title I resolution planning requirements to smaller BHCs whose failure could adversely impact financial stability—as assessed on the basis of non-size related criteria (e.g., interconnectedness, substitutability and complexity), in line with international good practices.²¹⁷</p> <p>Banking. Similarly to the approach taken under the DFA, the requirement for IDIs to prepare plans that should enable the FDIC to resolve the institution under the FDI Act is based on asset size, with a threshold of \$50 billion or more. Neither the FDIA, nor the IDI Rule, provides the FDIC with discretion to apply resolution planning requirements to smaller BHC whose failure could adversely impact financial stability—as assessed on the basis of non-size related criteria (e.g., interconnectedness, substitutability and complexity).</p> <p>State Insurance. State commissioners are becoming more involved in the recovery and resolution planning process. State commissioners are active in supervisory colleges and CMGs and beginning to review resolution plans and consult with the FRB/FDC in this process; however, resolution planning for systemically important insures would benefit from more coordination between FRB/FDIC and the states.</p> <p>Findings. Resolution planning requirements under DFA (including the 165(d) Rule) and the FDIA (including the IDI Rule) extend to non G-SIBs that could have an impact on financial stability in the event of their failure. For BHCs and IDIs, the applicability of the requirements is solely being based on asset size. The statutes do not provide for the agencies with discretion to apply the requirements to banking groups that do not meet the asset threshold of \$50 billion but whose failure may still have adverse implications on financial stability, for example in view of their interconnectedness; substitutability; and complexity.</p> |
| EC11.3 | <p>The legal framework imposes the responsibility for the development and maintenance of firms’ recovery planning process on the board and senior management, subject to regular review by supervisory or resolution authorities. Maintenance includes reviewing and updating the recovery plan at least annually, and sooner in the event of material changes to the firm’s business or structure.</p> |
| Description and findings re EC11.3 | <p>DFA. The U.S. agencies place responsibility for the recovery planning process on the firm’s senior management. The Board of Directors is responsible for the preparation, oversight and, where necessary, timely implementation of the recovery plans. Hence, firms’ boards of directors need to continuously keep stock of the firm’s ability to effectively identify and implement recovery options, and oversee the remediation of weaknesses identified in the firm’s processes.</p> |

²¹⁷ Also see guidance issued by the Basel Committee on Banking Supervision on the identification of domestic systemically important firms, <http://www.bis.org/publ/bcbs233.pdf>

Firms preparing recovery plans are required to ensure that the planning process is integrated into the firm's corporate governance and operating processes, with senior management being responsible for this integration.²¹⁸ Successful integration of recovery planning into the existing firm processes should result in:

- (i) timely recognition of financial weakness by the firm's management and analysis of the underlying cause of the weakness;
- (ii) timely discussion by management about the ability of the firm to respond to financial weakness and to address the long-term viability of the firm;
- (iii) timely notification of identified weakness to the Federal Reserve and other relevant supervisors;
- (iv) timely escalation by management of identified weaknesses and planned responses to the firm's board of directors; and
- (v) timely implementation of options or other remediating actions in a stress situation.

At a minimum, the firm's internal governance should lead to a response from the firm prior to the imposition of remedial actions by the Federal Reserve or other responsible supervisors. A firm should aim to have the ability to take timely action to address signs of weakness or risk before the onset of significant financial deterioration.

Banking. Board and senior management of IDIs that are subject to recovery planning requirements are responsible for the preparation and maintenance of such plans.

State Insurance. There are no provisions under state law expressly tasking the board and senior management of insurance companies with the development and maintenance of firms' recovery planning, as there are no explicit statutory requirements for recovery planning. Nevertheless, some information from regular ERM (Enterprise Risk Management) and ORSA (Own Risk and Solvency Assessment) reporting which is provided to the board, the senior management and the insurance commissioner may be useful in recovery planning processes.

Findings. As part of the FRB's framework for the consolidated supervision of large financial institutions, discussed in more detail in EC11.4 below, recovery plans are to be prepared by the largest, most complex U.S. and foreign institutions that are subject to consolidated supervision by the Federal Reserve, which include the U.S. based G-SIBs and G-SIIs; LBOs with consolidated assets of at least \$50 billion (to the extent not already included in the first category); and Large FBOs with combined assets of U.S. operations of at least \$50 billion (again, to the extent not already included in the first category). Covered firms are expected to ensure that their recovery planning is sufficiently integrated into corporate governance structures and processes, subject to independent validation, and effectively supported by related Management Information System (MIS) reporting to the board and its committees.

Further guidance on recovery plans, issued by the FRB in September 2014, applies to the eight U.S. based G-SIBs only. This guidance (again) clarifies that the planning process should be integrated into firms' corporate governance structures and processes, subject to independent validation, and effectively supported by related MIS reporting to the board and its committees. Boards of Directors are responsible for the preparation, oversight and, where necessary, timely implementation of the recovery plans.

²¹⁸ Supervisory Expectations for Recovery and Resolution Preparedness for Certain Large Bank Holding Companies (SR 14-1), <http://www.federalreserve.gov/bankinfo/reg/srletters/sr1401.pdf>

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| EC11.4 | <p>The legal framework requires recovery plans to:</p> <ul style="list-style-type: none"> (i) include measures for addressing capital shortfalls and liquidity pressures; (ii) set out credible recovery options to deal with a range of stress scenarios covering both idiosyncratic and market wide stress; and (iii) define clear backstops and escalation procedures, identifying the quantitative and qualitative criteria that would trigger implementation of the plan by the firm. |
| Description and findings re EC11.4 | <p>DFA. In December 2012, the FRB announced a new framework for the consolidated supervision of large financial institutions,²¹⁹ combining traditional microprudential supervision and regulation—aimed at ensuring the safety and soundness of individual firms—with macroprudential considerations that seek to reduce potential threats to the stability of the financial system as a whole.²²⁰</p> <p>The consolidated supervision framework has two primary objectives, i.e. (a) enhancing resilience of individual firms to lower the probability of failure or its inability to serve as an effective financial intermediary; and (b) reducing the impact on failures on the financial system and the broader economy. Such objectives are consistent with key provisions of the DFA, notably the authority provided to the FRB to apply enhanced prudential standards to NBFCs and BHCs with total consolidated assets of at least \$50 billion—in view of the risks to financial stability that may arise from a failure of such firms.</p> <p>The U.S. authorities view recovery planning as a central element to ensuring the ongoing resiliency of a firm’s consolidated operations and, in turn, lower the probability of its failure or inability to serve as a financial intermediary. In this context, the afore-mentioned firms are expected to prepare a plan for remedying potential financial or operational weaknesses and identify predefined recovery options. In this context, the firms are expected to</p> <ul style="list-style-type: none"> (i) maintain clearly documented quantitative and qualitative criteria that would trigger timely implementation of specific elements of the firm’s recovery plan and provide for more rigorous remediation activities if initial actions prove insufficient; (ii) ensure that trigger events reflect a sufficiently broad range of market- and firm-specific stresses across financial, operational, reputational, legal, and compliance risks; (iii) ensure that recovery planning reflects a holistic view of sustainability and resiliency. Recovery planning should be closely integrated with resolution planning, capital and liquidity planning, and other aspects of financial contingency, crisis management, and business continuity planning; (iv) undertake recovery testing and training exercises that consider a broad range of internal and external risk scenarios and account for interconnectivities across operations and legal entities; (v) ensure that the recovery plan is updated as needed, and reflects lessons learned from reviews of trigger events, testing, and training exercises; and (vi) ensure that recovery planning is sufficiently integrated into corporate governance structures and processes, subject to independent validation, and effectively supported |

²¹⁹ Consolidated Supervision Framework for Large Financial Institutions (SR 12-17), <http://www.federalreserve.gov/bankinforeg/srletters/sr1217.pdf>.

²²⁰ DFA Section 165 (a)(2).

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| | <p>by related MIS reporting to the board and its committees</p> <p>In accordance with further guidance from the FRB,²²¹ G-SIBs are expected to implement a recovery planning process that is capable of determining a range of remedial actions that the firm could take to remedy financial weakness and maintain market confidence without extraordinary governmental support—with the range of options including, at a minimum, the possible sale, transfer, or disposal of significant assets, portfolios, legal entities, or business lines.</p> <p>To ensure that recovery options are actionable, including under scenarios of distress, the planning process should highlight potential impediments to their execution and present mitigation strategies. Moreover, it should identify a comprehensive range of recovery options that can be deployed under a broad range of internal (e.g., significant losses, portfolio shocks, fraud, major failures of the firm’s corporate governance and risk management framework) or external stresses (e.g., severe changes in debt or equity valuations, currency or interest rates, and a sudden collapse of market liquidity). The stresses should reflect a variety of market and economic conditions, consider tail-events that could bring the firm nearest to entering resolution proceedings, and develop options for recovery from such circumstances.</p> <p>To be effective, recovery planning should be integrated into a firm’s corporate governance and operating processes, including firm-wide risk-management processes. Firms’ recovery options should be kept current in order to position the firm to respond to changing challenges. At minimum, firms should review and update their recovery plans on an annual basis, with such a review analyzing whether there have been changes to the firm’s structure or to external conditions that would materially impact the execution of recovery options in the plan.</p> <p>Aspects to be addressed in firms’ recovery plans include the following</p> <ul style="list-style-type: none"> (i) Internal Governance: the recovery plan should describe the governance framework for recovery planning, including a description of how the plan is developed, approved, and updated. In particular, the plan should outline how the plans links with the firm’s contingency, strategic and resolution planning efforts; and describe triggers for initiating recovery measures, along with related escalation procedures for senior management action and notification of board of directors. (ii) Recovery Options: the recovery plan should detail options for remedying financial weakness and maintaining market confidence in the firm without extraordinary governmental support. The options in the plan should be actionable and comprehensive, and should include: options to conserve or restore liquidity and capital; opportunities and strategies to de-risk and de-lever the firm; options contemplating the sale, transfer, or disposal of significant assets, portfolios, legal entities, or business lines; and options that may permanently change the firm’s structure or business strategy. (iii) Execution Plan: for each recovery option listed, the recovery plan should describe the steps necessary to execute the option. Among others, the description should highlight the estimated time frame for implementation; a description of any impediments to execution of the option and mitigation strategies to address those impediments; and a plan describing the methods and forms of communication with internal, external, and |
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²²¹ Consolidated Recovery Planning for Certain Large Domestic Bank Holding Companies (SR 14-8), <http://www.federalreserve.gov/bankinfo/srletters/sr1408.pdf>

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| | <p>regulatory stakeholders.</p> <p>(iv) Impact Assessment: the recovery plan should holistically consider and describe the expected impact of individual recovery options. At a minimum, this should include a financial impact assessment that describes the impact of executing each option on the firm’s capital, liquidity, and balance sheet; a business impact assessment that describes the effect of executing each option on business lines and material entities; and an analysis of the potential consequences or recovery actions on counterparties, creditors, clients, depositors and markets for specific assets.</p> <p>Banking. The FBAs have not issued separate recovery planning requirements for IDIs. However, bank supervisors expect that banks integrate recovery planning into their overall governance framework and risk management processes. While the afore-mentioned framework for consolidated framework comprises LBOs with consolidated assets of at least \$50 billion, the more granular guidance that was issued by the FRB in 2014 is only applicable to the U.S. based G-SIBs.</p> <p>State Insurance. There are no statutory requirements under state law regarding recovery planning by insurance companies. Neither the NAIC’s Risk Management and Own Risk and Solvency Assessment Model Act (# 505), nor the related ORSA Guidance Manual of the NAIC prescribe requirements for recovery planning. Nevertheless, insurance companies may include aspects of recovery planning in their regular ERM and ORSA reports pursuant to the relevant state’s adoption of section 5 of this Model Act.</p> <p>Findings. The consolidated supervisory framework for large financial institutions, announced by the FRB in 2012, comprises, amongst others, recovery planning requirements. However, the scope of applicability of the granular supervisory guidance that was issued in September 2014 is explicitly limited to the eight U.S. based G-SIBs. Hence, there is some ambiguity as to the exact requirements that apply to smaller institutions.</p> |
| <p>EC11.5</p> | <p>The resolution regime sets out the requirements for the content of resolution plans which, at a minimum, include a substantive resolution strategy and an operational plan that meets the requirements set out in points (i) to (vi) of KA 11.6 (for all firms) and, additionally, for insurers, paragraph 9.10 of II-Annex 2 on Resolution of Insurers.</p> |
| <p>Description and findings re EC11.5</p> | <p>DFA. Since the formal adoption of the DFA in 2010, the agencies have issued multiple documents that lay out supervisory expectations and/or formal rules pertaining to firms’ living wills, as prepared under Title I.</p> <p>(i) 165(d) Rule. Plans for the orderly resolution under the U.S. Bankruptcy Code, as required under Title I of the DFA, should include, at minimum, a strategic analysis describing the covered company’s plan for rapid and orderly resolution in the event of material financial distress; the company’s corporate governance arrangements for resolution planning; a description of the company’s organizational structure; a detailed inventory of the company’s MIS; an analysis of interconnections and interdependencies that, if disrupted, could negatively affect the company’s operations; and an overview of relevant supervisory agencies in the U.S. and abroad. Moreover, the plans need to reflect three scenarios of distress, i.e. a baseline scenario, an adverse scenario and a severely adverse scenario—with the latter reflecting the economic conditions that are provided by the FRB pursuant to stress testing requirements under the DFA. The 165(d) Rule explicitly precludes covered institutions</p> |

from relying “on the provision of extraordinary support by the U.S. or any other government (...) to prevent the failure of the covered company”.²²² The additional requirements for insurance companies as set out in paragraph 9.10 of II-Annex 2 on Resolution of Insurers are not covered by the 165(d) Rule yet.

(ii) **Supervision and Regulation (SR) letter 12-17.** The consolidated supervision framework that the FRB presented in 2012 provides, in addition to recovery planning (see EC 11.4), an overview of the key aspects that the FRB and FDIC analyze as part of their review of the plans’ adequacy including:

- a) The firm’s strategic analysis describing its plans for rapid and orderly resolution under the U.S. Bankruptcy Code (or other relevant insolvency regimes).
- b) The firm’s strategy for maintaining and funding material entities, critical operations, and core business lines in the event of material financial distress.
- c) Analysis of potential impediments to resolution, and actions to make the firm more resolvable or otherwise reduce its complexity and interconnectivity.
- d) Analysis of whether the failure of a major counterparty would likely result in the material financial distress or failure of the firm.
- e) The manner and extent to which an insured depository subsidiary is adequately protected from risks arising from the activities of non-depository subsidiaries.
- f) For a U.S. firm with foreign operations, its strategy for addressing the risks arising from these foreign operations to its U.S. operations, and its ability to maintain core business lines and critical operations in foreign jurisdictions.
- g) Analysis of whether resolution planning is sufficiently integrated into corporate governance structures and processes, subject to independent validation, and effectively supported by related MIS reporting to the board of directors and its committees.

(iv) **2013 Resolution Plan Guidance.** Following the publication of the aforementioned documents, the agencies published additional guidance, clarification and direction for the so-called “first wave filers” (i.e. BHCs with consolidated assets of \$250 billion or more) in April 2013.²²³ Among others, the guidance mandates covered companies to (a) provide the strategic analysis in the form of a concise narrative that enhances the readability and understanding of the company’s strategy for rapid and orderly resolution under bankruptcy proceedings; (b) discuss a number of obstacles to rapid and orderly resolution that the agencies have identified in their reviews of the July 2012 plans, and provide the actions taken to remediate or otherwise mitigate each obstacle; and (c) discuss the process that covered companies would undertake to commence bankruptcy proceedings.

(iv) **SR letter 14-1.** In January 2014, the FRB specified, as a supplement to SR letter 12-

²²² 12 CFR § 243.4(a)(4)(ii).

²²³ <http://www.federalreserve.gov/newsevents/press/bcreg/20130415c.htm>

17, heightened supervisory expectations for recovery and resolution preparedness for the eight U.S.-based G-SIBs.²²⁴ In particular, the letter specifies a range of capabilities that are deemed critical to firms' operational resilience and contingency planning in circumstances where capital and liquidity buffers are strained, and to the resiliency of the financial system as a whole.

- a) Effective processes for managing, identifying, and valuing collateral it receives from and posts to external parties and affiliates;
- b) A comprehensive understanding of obligations and exposures associated with payment, clearing, and settlement activities;
- c) The ability to analyze funding sources, uses, and risks of each material entity and critical operation, including how these entities and operations may be affected under stress;
- d) Demonstrated management information systems capabilities for producing certain key data on a legal entity basis that is readily retrievable and controls in place to ensure data integrity and reliability; and
- e) Robust arrangements in place for the continued provision of shared or outsourced services needed to maintain critical operations that are documented and supported by legal and operational frameworks.

Banking. The IDI Rule,²²⁵ adopted by the FDIC in 2011, prescribes similar requirements as those envisaged in the 165(d) Rule, albeit with a more narrow objective, i.e. the protection of insured depositors and the FDIC's deposit insurance fund. In essence, the Rule aims to support the maximization of the net present value return from the sale or disposition of the filed IDI's assets, while minimizing the amount of any loss realized by the creditors in resolution.²²⁶

On substance, IDI plans should include an overview of the covered IDI's structure (including its legal entities, core business lines and branches); its corporate governance; critical services, key service providers and modalities to ensuring continuity in the event of a failure; the payment, clearing and settlement systems of which the IDI is a member, the interconnectedness with the IDI's parent company and its legal entities, as well as interconnections and interdependencies that could hinder the timely resolution of the IDI; the IDI's major counterparties and the estimated implications of a failure of such counterparties on the IDI; material off balance sheet exposures and pledged collateral; the IDI's capital structure and its funding sources, including affiliate funding relations; its systemically important functions; and its management information systems.

In terms of resolution strategies, the IDI plan should, at minimum, discuss how it can be effectively separated from its parent company; and how its branches, core business lines and major assets can be sold in a manner that ensures that depositors receive access to their insured deposits within one day of the IDI's failure. Moreover, the plan should describe how the strategies for such separation can be demonstrated to be the least costly to the deposit

²²⁴ <http://www.federalreserve.gov/bankinforeg/srletters/sr1401.pdf>

²²⁵ 12 CFR § 360.

²²⁶ 12 CFR § 360.10(a).

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| | <p>insurance fund of all possible resolution methods.</p> <p>The FDIC's guidance for the 2015 IDI plans,²²⁷ released in December 2014, provided further detail on the FDIC's expectations pertaining to IDIs submissions. Among others, it clarifies that the "failure scenario" that should be reflected in the plans—in essence requiring the financial condition of the covered IDI should reflect an insolvency-based ground for receivership under the FDIA—and on resolution strategies that should be analyzed (i.e. at least one strategy that primarily involves the separation and sale of the covered IDI's deposit franchise, core business lines, and/or major assets to multiple acquirers; and one strategy that involves the liquidation of the firm, including a payout of insured deposits). Finally, the guidance asks covered IDIs to identify critical services (defined as services and operations of the firms that are necessary to continue the day-to-day operations, such as servicing, information technology, support and operations, human resources and personnel) and discuss how such services can be effectively maintained in resolution.</p> <p>State Insurance. There are no statutory requirements under state law regarding resolution planning by insurance companies. Nevertheless the information from regular ERM and ORSA reporting which is provided to the board, the senior management and the insurance commissioner pursuant to state's adoption of section 5 of NAIC's Risk Management and Own Risk and Solvency Assessment Model Act (# 505) can be used in the resolution planning processes</p> <p>Findings. The rules and guidance pertaining to the 165 (d) requirements, together with the minimum requirements for resolution plans of covered IDIs (as per the IDI rule), broadly cover the elements mentioned in KA 11.6. It should be noted that any discussion of exit scenarios under 165(d) requirements relate to the exit from Bankruptcy proceedings, rather than the resolution process—due to the fact that living wills that are required under 165(d) assume resolution under the U.S. Bankruptcy Code, rather than via a special resolution regime (such as the OLA established under DFA's Title II).</p> <p>Regarding the U.S. based G-SIIs, requirements and guidance provided by the 165(d) Rule and SR letter 12-17 apply in full, while the scope of application of the 2013 Resolution Plan Guidance and SR letter 14-1 does not include NBFCs. In addition, state law does not provide requirements for insurance groups whose failure could have adverse effects, at a domestic level, on financial stability and the broader economy.</p> |
| EC11.6 | <p>If the jurisdiction is home to a G-SIFI, or any other firm that could, in the judgment of its home authority, have an impact on financial stability in the event of its failure, the home resolution authority has a process in place for the authorities represented on the CMG or equivalent arrangement to review the substantive resolution strategy for the firm and for the agreement of that strategy by top officials of those authorities.</p> |
| Description and findings re EC11.6 | <p>DFA. As highlighted above, the FDIC, as the home resolution authority, is in the process of developing resolution strategies under Title II, where appropriate informed by the firms' submissions under Title I. The FDIC has presented an update on firm-specific Title II resolution strategies for the U.S.-based G-SIBs at CMG meetings that took place in Q4-2014. The FDIC has also engaged CMG members on a bilateral basis regarding substantive resolution issues. Illustrative thereof is the work done between the FDIC and the Bank of England in 2012,</p> |

²²⁷ <https://www.fdic.gov/news/news/press/2014/pr14109.html>

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| | <p>culminating in a joint paper on the application of “top down” (SPE) resolution strategies for U.S.-based and UK-based G-SIBs.²²⁸</p> <p>With regard to insurance groups, the development of resolution strategies for NBFCs that have been designated by the FSOC is in the preliminary stage. Hence, the inaugural meetings of the CMGs for AIG and Prudential that took place in Q4-2014 did not provide for comprehensive discussions on resolution strategies for both firms, as those plans were still under review by the FRB and FDIC. State regulators have been informed by federal authorities that consultation on the review of the resolution plans will occur prior to discussions with the relevant institutions.</p> <p>Banking. The FDI Act does not contain any provisions on coordination with foreign authorities in the context of resolution planning.</p> <p>State Insurance. There are no provisions under state law regarding resolution planning by insurance companies.</p> <p>Findings. The FDIC is in the process of developing resolution strategies under DFA Title II, factoring in—where appropriate—the firms’ own plans under Title I. The main modalities of the firm-specific strategies are being discussed in CMG-meetings of the U.S.-based G-SIBs. The preparation of resolution strategies for covered NBFCs is less advanced.</p> |
| <p>EC11.7</p> | <p>The resolution regime requires firms to ensure that their Service Level Agreements that are required to maintain continuity of critical functions or critical shared services can be maintained in crisis situations and in resolution, and that the underlying contracts include provisions that prevent termination from being triggered by recovery or resolution events and facilitate transfer of the contract to a bridge institution or a third party acquirer.</p> |
| <p>Description and findings re EC11.7</p> | <p>DFA. Firms subject to recovery and resolution planning requirements are expected to take all necessary arrangements to ensure the continuation of services that are necessary to maintain critical operations and shared services, including by entering into robust service level agreements. In accordance with the FRB’s heightened supervisory expectations for U.S.-based G-SIBs, said firms are required to establish robust arrangements in place for the continued provision of shared or outsourced services needed to maintain critical operations that are documented and supported by legal and operational frameworks.²²⁹ Among others, firms should</p> <ul style="list-style-type: none"> (i) evaluate internal and external dependencies and develop documented strategies and contingency arrangements for the continuity or replacement of the shared and outsourced services that are necessary to maintain critical operations; and (ii) maintain current cost estimates for implementing such strategies and contingency arrangements. <p>The legal framework does not provide for detailed (minimum) standards for critical functions and shared services of FSOC designated NBFCs; the aforementioned supervisory letter solely applies to U.S.-based G-SIBs.</p> <p>Banking. External providers of critical functions of a failed financial institution are prohibited from exercising any right to terminate, accelerate or declare a default under relevant service level agreements; obtaining or taking possession, or exercising control over, any property of a failed</p> |

²²⁸ <https://www.fdic.gov/about/srac/2012/gsifi.pdf>

²²⁹ Supervisory Expectations for Recovery and Resolution Preparedness for Certain Large Bank Holding Companies (SR 14-1).

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| | <p>institution; or affect any contractual rights of the failed institution without the consent of the FDIC during the 90-day period commencing on the date of appointment of the FDIC as receiver.²³⁰</p> <p>State Insurance. Section 108 C. of IRMA prohibits the termination of any contract solely on the basis that receivership proceedings have been commenced against the insurer. Previous model laws do not contain a similar prohibition and it is unclear to what degree such a provision has been incorporated into the legislation of relevant states.</p> <p>Findings. Firms subject to resolution planning under DFA 165(d) are expected to take all necessary arrangements to ensure the continuation of services that are necessary to maintain critical operations and shared services. There are no binding standards on critical functions and shared services of FSOC designated NBFCs.</p> |
| EC11.8 | <p>If the jurisdiction is home to a G-SIFI the resolution authority has a process in place to develop a group-wide resolution strategy and plan for the G-SIFI in coordination with all members of the firm's CMG, and gives all members of the CMG access to the firm's RRP and information on measures that would have an impact on their jurisdiction.</p> |
| Description and findings re EC11.8 | <p>DFA. As highlighted under EC11.1, the FDIC has been developing its capabilities for effecting an orderly resolution under Title II since the enactment of the DFA. Updates on the firm-specific resolution strategies have been presented during the CMG meetings for the U.S.-based G-SIBs that took place in Q4-2014 (see EC 11.6). The U.S. authorities' template includes an explicit commitment to lead the development of the group-wide resolution strategy, to be reviewed in the relevant CMG (also see EC 9.1) The FRB and FDIC have not instituted a procedure for sharing, at their own initiative, the firm-specific plans for effecting rapid and orderly resolution under the U.S. Bankruptcy Code, prepared pursuant to DFA section 165(d), but have generally made key information available to CMG members upon request.</p> <p>With regard to the U.S.-based G-SIIs, a process for the development of group-wide resolution strategies has not yet been developed. As such, the inaugural CMG meetings for the U.S.-based G-SIIs, which took place in Q4-2014, did not include a discussion of the FDIC's group-wide resolution strategies. At their request, the U.S. authorities have generally provided CMG members with information on the firms' living wills, prepared pursuant to DFA Title I.</p> <p>State Insurance. There is no specific statutory requirement under state law for a process to develop a group-wide resolution strategy with all CMG members.</p> <p>Findings. Updates on firm-specific resolution plans, developed by the FDIC under Title II, are being shared with CMG members. The development of such plans, however, is more advanced for U.S.-based G-SIBs than for the FSOC designated NBFCs. Regarding the U.S. based G-SIIs, a process or the development of group-wide resolution strategies has not yet been established.</p> |
| EC11.9 | <p>If the jurisdiction is home to a G-SIFI, the home resolution authority has a process in place to cooperate with authorities of jurisdictions where the G-SIFI has a systemic presence that are not members of the CMG, and provide authorities in those jurisdictions with access to relevant material from the RRP and information on resolution strategies or measures that the home resolution authority judges would have an impact on their jurisdiction.</p> |
| Description and findings | <p>DFA. As highlighted under KA 8.3, the agencies have taken a variety of steps to facilitate cross-border cooperation with host supervisors, including via establishment of colleges of supervisors</p> |

²³⁰ FDI Act 12 USC. § 1821(e)(13)(C)(i) and DFA Section 210(c)(13)(C)(i).

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| re EC11.9 | <p>and bilateral memoranda of understanding. Pending the finalization of draft FSB guidance on cooperation and information sharing with non-CMG hosts, the agencies have not yet instituted formal procedures on the interaction concerning resolution-related matters with host authorities from jurisdictions that are not represented on CMGs, but where U.S. G-SIFIs have a systemic presence. They intend, however, to align their engagement with such hosts with the guidance, once it is finalized.</p> <p>Banking. The FDI Act does not include specific statutory provisions that relate to the interaction with non-CMG hosts.</p> <p>State Insurance. There is no specific statutory requirement under state law for a process for the cooperation with foreign non-CMG-member authorities.</p> <p>Findings. The agencies have stated their intent to realign their engagement with host authorities from jurisdictions that are not represented on CMGs, but where U.S. G-SIBs and G-SIIs have a systemic presence once relevant FSB guidance has been finalized.</p> |
| EC11.10 | <p>If the jurisdiction under review is a host to a firm that is subject to a requirement for a group-wide resolution plan and maintains its own resolution plans for the firm's operations in its jurisdiction, there is a clear process for coordination with the home authority to ensure that the plan is as consistent as possible with the group plan.</p> |
| Description and findings re EC11.10 | <p>DFA. As highlighted under EC 11.1, all BHCs with consolidated assets equal or greater than \$50 billion are required to provide the FRB and FDIC with plans for their orderly resolution under the U.S. Bankruptcy Code. This group includes local operations from G-SIBs domiciled abroad, e.g., in France, Germany, Japan, Spain, Switzerland and the United Kingdom. To the extent that the agencies participate in CMGs of the relevant institutions, they are able to contribute to the group-wide resolution plan of the relevant firms, injecting their understanding of the potential impediments to effective resolution that have been identified at the level of the U.S. operations.</p> <p>While there is nothing precluding the FRB and FDIC from sharing, at own initiative, the firm-specific Title I plans, and materials have in fact been provided at the request of CMG members (as highlighted in EC 11.9), the agencies have not institutionalized any procedures for proactively sharing these documents with home authorities. Where available, the agencies' input on group-wide resolution strategies and resolvability assessments is based on title II resolution strategies. Inherently, such strategies allow for better alignment with group-wide plans than the firms' Title I plans, as the latter focus on rapid and orderly resolution of the firm under U.S. bankruptcy law.</p> <p>Although the FSOC has, to date, not exercised its authority under DFA section 113 to designate the U.S. operations of a foreign insurance group as relevant for financial stability in the U.S.—subjecting the firm to FRB supervision and resolution planning requirements under Title I—the FSOC would, in principle, be mandated to also issue such determinations for foreign-owned entities, based on its assessment on the systemic importance of their U.S. operations.</p> <p>Banking. Similarly, the group of IDIs that is required, pursuant to the FDIC's IDI Rule, to submit plans for the orderly resolution of such institutions in the event of failure contains a number of institutions that is owned by foreign banking groups. To the extent that the FDIC participates in CMGs or similar fora for the relevant groups, the FDIC is effectively able to leverage these plans when contributing to the development of group-wide resolution plans.</p> <p>State Insurance. There is no specific requirement under state law for setting up a resolution plan for the domestic business operations of a foreign insurance company.</p> <p>Findings. The U.S. authorities' participation in CMGs of foreign G-SIFIs with material</p> |

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| | operations in the U.S. allows for a consistency check of host and home resolution strategies. However, the firms' living wills under Title I are less suited for full alignment with the group-wide plans, due to their focus on resolution under the U.S. Bankruptcy Code. |
| EC11.11 | The resolution regime requires authorities to review and, to the extent necessary, update resolution plans at least annually, and sooner upon the occurrence of an event that materially changes the firm's business or structure, including its operations, strategy or risk exposure. |
| Description and findings re EC11.11 | <p>DFA. The 165(d) Rule requires covered companies to file plans for their orderly resolution under the U.S. Bankruptcy Code with the FRB and FDIC on an annual basis. Except in situations where the FRB and FDIC granted extensions, firms have been submitting their plans in accordance with the staggered submission schedule that has been introduced under the Rule²³¹ (see KA 11.1).</p> <p>The Rule provides for interim updates, to be requested by the agencies on the basis of a joint decision, and a requirement for covered companies to inform the agencies within a 45 day timeframe about any event, occurrence, or other change that results in, or could reasonably be foreseen to have, a material effect on the plan of the covered company. Such company is required to incorporate said event, occurrence, or other change in the following plan. Moreover, the Rule authorizes the agencies, based on a joint decision, to request plans more frequently than the annual cycle, or extend the time period that companies have to provide an updated submission, following material events.</p> <p>Banking. The IDI Rule contains similar provisions, i.e. annual submissions on the basis of a staggered submission schedule, discretion for the FDIC to modify submission dates and a mandatory reporting of material events.²³²</p> <p>State Insurance. There is no specific provision under state law for reviewing a resolution plan of an insurance company.</p> <p>Findings. Firms are required to submit Title I and IDI resolution plans on an annual basis, with the authorities having discretion to impose alternative submission dates. Material events have to be notified to the agencies within 45 days after the event. In contrast with the 165(d) Rule, the FDIC's IDI rule does not explicitly provide for the authority to request interim updates.</p> |
| EC11.12 | <p>If the jurisdiction under review is home to a G-SIFI, it has in place a process for coordination with authorities participating in the CMG for the review, at least annually, of:</p> <p>(i) the resolution strategy by top officials of home and relevant host authorities, involving the firm's CEO where appropriate; and</p> <p>(ii) the operational plans for the implementation of resolution the strategy by senior officials of the relevant (home and host) authorities.</p> |
| Description and findings re EC11.12 | <p>DFA. The U.S. authorities are utilizing CMGs, both for U.S.-based G-SIBs and G-SIIs to coordinate group-wide resolution strategies and resolvability assessments. The ongoing Resolvability Assessment Process, conducted under the leadership of the FSB and guided by technical discussions in the various CMGs, includes interaction with firms' senior officials on impediments to resolvability, and potential mitigations thereof.²³³</p> <p>With regard to the NBFs, however, engagement of foreign authorities is in an early stage, as</p> |

²³¹ 12 CFR § 243.3(a)(3).

²³² 12 CFR § 360.10(c).

²³³ http://www.financialstabilityboard.org/wp-content/uploads/r_130902.pdf

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| | <p>the agencies are still in the process of finalizing resolution strategies.</p> <p>Banking. The FDI Act does not include specific provisions that relate to coordination with CMG members.</p> <p>State Insurance. There is no specific requirement under state law for establishing a process for the review of the resolution strategy and the operational plan for the implementation of the resolution strategy of an insurance company.</p> <p>Findings. The U.S. authorities are engaging foreign authorities on group-wide resolution strategies and resolvability assessments, as these become available, via the CMG.</p> |
| EC11.13 | <p>The supervisory or resolution authority has the power to require a firm to take measures to address deficiencies in its recovery plan or inputs to their resolution plan, and in cases where authorities require firms to prepare an initial resolution plan, its initial resolution plan.</p> |
| Description and findings re EC11.13 | <p>DFA. Pursuant to DFA section 165(d) and the 165(d) Rule, the FRB and the FDIC are required to review institutions’ plans for the orderly resolution under the U.S. Bankruptcy Code, with the aim to determine whether the plan is “credible” or would otherwise “facilitate an orderly resolution of the company under the U.S. Bankruptcy Code”. Should the agencies jointly decide that a plan does not meet this requirement, and should the covered company prove unable to resubmit its plan with revisions demonstrating that it is credible and would result in orderly resolution, the FRB and FDIC may jointly impose more stringent capital, leverage or liquidity requirements or restrictions on growth, activities or operations, until such time that the company resubmits a plan that remedies the noted deficiencies. As highlighted in EC10.3, failure to resubmit an acceptable plan within two years from the imposition of the afore-mentioned measures, may result in an instruction from the agencies, in consultation with the FSOC, to divest certain assets or operations to facilitate an orderly resolution.</p> <p>The concept of “credibility” is not defined in the DFA, nor elaborated in the 165(d) Rule, providing the agencies with broad discretion.</p> <p>Banking. The IDI Rule prescribes that the FDIC shall review the resolution plans of covered IDIs, with the aim to determine whether the plan is credible at providing strategies for resolving the covered IDI, and the detailed information required under the IDI Rule, that are “well-founded and based on information and data related to the covered IDI that are observable or otherwise verifiable, and employ reasonable projections from current and historical conditions with the broader financial markets”.²³⁴</p> <p>The FDIC is required to inform the covered IDI in writing if it finds that an IDI plan is incomplete, or that additional information is necessary to facilitate a review of the plan. The covered IDI, in turn, shall resubmit the revised plan, or such additional information, no later than 30 days from the receipt of the FDIC’s notice.</p> <p>A substantive review of the plan shall be performed by the FDIC, in consultation with the appropriate FBA. If the FDIC then concludes that the plan is not credible, the covered IDI shall be requested to submit a revised plan within 90 days or receiving notice—or within a shorter or longer period, as the FDIC may determine. The IDI Rule, however, does not explicitly identify the potential consequences of a failure to correct noted deficiencies in a resolution plan.</p> <p>State Insurance. There is no specific statutory requirement under state law regarding measures to address deficiencies in resolution plans.</p> |

²³⁴ 12 CFR § 360.10(c)(4)(i).

Findings. The DFA provides the FRB and FDIC with explicit powers to address deficiencies in companies’ resolution plans, allowing the agencies to take far-reaching measures. The IDI Rule is silent on remedial actions, requiring the FDIC (as also highlighted in EC10.3) to deploy its general enforcement powers under the FDIA.

Assessment of KA11

Comments

The U.S. authorities have established a comprehensive regulatory framework for the development of living wills that seeks to facilitate the rapid and orderly resolution under Title 11 of the U.S. Bankruptcy code of complex financial institutions in the event of material financial distress or failure. The requirements—which apply to (a) all BHCs with consolidated assets of at least \$50 billion; (b) two of the three U.S. based G-SIIs (via the FSOC designation process); and (c) IDIs with total assets of \$50 billion or more—require each covered company to produce a plan that provides the FDIC with a thorough understanding of their structure and complexity, as well as their resolution strategies and processes. In doing so, the plans support the FDIC’s planning for the exercise of its authority under the OLA, and the FDI Act as appropriate, and otherwise will assist the agencies in their supervisory efforts to ensure that the covered companies operate in a manner that is considered safe and sound, and does not pose risks to financial stability. In addition, the plans enhance the agencies’ understanding of the U.S. operations of foreign banks and thus improve efforts to develop comprehensive and coordinated group-wide resolution strategies for cross-border firms.

Since the enactment of the agencies’ final rules in 2011, further guidance has been provided on various aspects pertaining to recovery and resolution planning, including on supervisory expectations for recovery planning, assumptions and scenarios that the covered companies should incorporate in their plans, key impediments to resolvability and potential mitigating measures, and on minimum standards for recovery and resolution preparedness. Taken as a whole, the guidance is broadly in line with FSB requirements, even though it is noted that minimum standards for recovery and resolution plans of complex insurance groups remain underdeveloped.

In this context, the development of insurance-specific standards, leveraging FSB guidance (notably Appendix II, Annex 2 of the Key Attributes and draft guidance on the identification of critical functions and critical shared services, released on October 2014), is imperative. Such standards, in combination with thorough reviews of the submissions from all covered companies (focusing, in particular, on the remediation of previously identified shortcomings), as well as ongoing supervisory efforts to gauge the adequacy of companies’ capabilities to support recovery and resolution preparedness, should facilitate the robust implementation of the regulatory framework. Moreover, it should be considered to provide the agencies with the legal authority to request recovery and resolution plans from banks that do not meet the numeric asset threshold (currently set at \$50 billion) under Title I but that could, in view of other characteristics, nonetheless pose systemic risks. Finally, the FDIC is encouraged to continue efforts to ensure preparedness for resolutions on the basis of the FDI Act, thus opting for a belt-and-braces approach that provides additional safeguards in situations where the OLA cannot be deployed or where the SPE strategy may face implementation challenges.

12. Access to Information and Information Sharing

KA12.1 Jurisdictions should ensure that no legal, regulatory or policy impediments exist that hinder the appropriate exchange of information, including firm-specific information, between supervisory authorities, central banks, resolution authorities, finance ministries and the public authorities responsible for guarantee schemes. In particular:

- (i) the sharing of all information relevant for recovery and resolution planning and for

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| | <p>resolution should be possible in normal times and during a crisis at a domestic and a cross-border level;</p> <p>(ii) the procedures for the sharing of information relating to G-SIFIs should be set out in institution-specific cooperation agreements (see Annex I); and</p> <p>(iii) where appropriate and necessary to respect the sensitive nature of information, information sharing may be restricted, but should be possible among the top officials of the relevant home and host authorities.</p> |
| KA12.2 | <p>Jurisdictions should require firms to maintain Management Information Systems (MIS) that are able to produce information on a timely basis, both in normal times for recovery and resolution planning and in resolution. Information should be available at the group level and the legal entity level (taking into account information needs under different resolution scenarios, including the separation of individual entities from the group). Firms should be required, in particular, to:</p> <p>(i) maintain a detailed inventory, including a description and the location of the key MIS used in their material legal entities, mapped to their core services and critical functions;</p> <p>(ii) identify and address exogenous legal constraints on the exchange of management information among the constituent entities of a financial group (for example, as regards the information flow from individual entities of the group to the parent);</p> <p>(iii) demonstrate, as part of the recovery and resolution planning process, that they are able to produce the essential information needed to implement such plans within a short period of time (for example, 24 hours); and</p> <p>(iv) maintain specific information at a legal entity level, including, for example, information on intra-group guarantees and intra-group trades booked on a back-to-back basis.</p> |
| Essential criteria | |
| EC12.1 | The resolution authority has the power under the legal framework to access any information from firms that is material for the planning, preparation and implementation of resolution measures in a timely manner. |
| Description and findings re EC12.1 | <p>DFA. The FDIC has access to information that is material for the planning, preparation and implementation of resolution measures through its review, conducted jointly with the FRB, of plans submitted pursuant to Section 165(d)(1) of the DFA by NBFCs that could pose a threat to the financial stability of the U.S., as determined by the FSOC,²³⁵ and bank holding companies with \$50 billion or more in total consolidated assets. These plans are required to provide a broad range of information relevant to resolution planning and implementation including, for example, detailed descriptions of organizational structures, credit exposures and cross-guarantees, as well as supporting data.</p> <p>Once the FDIC has been appointed as receiver for a covered financial company, other federal regulators shall make available all records relating to such company.²³⁶</p> <p>The FDIC may also exercise its special examination authority with respect to any NBFC supervised by the FRB or BHC with total consolidated assets equal to or greater than \$50 billion for the purpose of implementing the FDIC's authority under Title II of the DFA, provided that the</p> |

²³⁵ DFA Sections 113(a)(1) and 165(d)(1).

²³⁶ DFA Section 210(i).

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| | <p>FDIC must coordinate any such special examination to the maximum extent practicable with the FRB and that such special examination authority may not be used with respect to any such NBFC or BHC that is in a generally sound condition.²³⁷</p> <p>Banking. As a general matter, the FDIC has access to firms' information in connection with its responsibility to conduct on-site examinations of IDIs and its authority to take enforcement actions against IDIs, bank holding companies, and affiliates thereof under statutorily prescribed conditions.²³⁸</p> <p>The FDIC also has special examination authority with respect to any IDI and it may exercise it whenever it determines that this is necessary to gauge the condition of such IDI for insurance purposes. In connection with the exercise of this special examination authority, the FDIC has the authority to examine the affairs of any affiliate of any IDI as may be necessary to disclose fully (i) the relationship between any such IDI and any such affiliate; and (ii) the effect of such relationship on the IDI.²³⁹</p> <p>The FDIC can also have access to firms' information through its review of plans submitted by IDIs with \$50 billion or more in total assets.</p> <p>State Insurance. Under state insurance holding company legislation, the commissioner as state regulator has access to the books, records and other information held by the insurer and its affiliates that may be utilized for establishing a crisis management plan.</p> <p>Under the IHCA, the commissioner as a regulator has the power to examine an insurer and its affiliates to ascertain the financial condition, including enterprise risk, of each of the insurer group companies and the insurer group as a whole.²⁴⁰ The commissioner may order any registered insurer to produce such records, books and other information papers in the possession of the insurer or its affiliates as are reasonably necessary to determine compliance with relevant regulations. The commissioner has the power to initiate the establishment of, or participate in, a supervisory college in order to determine compliance by the insurer subject to supervision.²⁴¹</p> <p>Findings. The FDIC has strong powers to access information that is material for the planning, preparation and implementation of resolution measures in a timely manner and through several legal avenues. When the FDIC does not have direct access to such information, it has in place robust information sharing mechanisms with the relevant federal regulatory agencies. Similar conclusions apply with respect to the information gathering powers of commissioners under state insurance resolution regimes.</p> |
| EC12.2 | <p>The legal framework permits and contains adequate legal gateways for the disclosure, in normal times and during a crisis, of non-public information (including firm-specific information) necessary for recovery and resolution planning and for carrying out resolution to domestic and foreign authorities that could have a role in resolution, including as appropriate supervisory authorities, central banks, resolution authorities, finance ministries and the public authorities responsible for guarantee schemes. Disclosure under those legal gateways is conditional on the</p> |

²³⁷ FDI Act, 12 USC. § 1820(b)(3) and (4).

²³⁸ FDI Act, 12 USC. §§ 1818(t) and 1820(d).

²³⁹ FDI Act, 12 USC. § 1820(b)(4)(A).

²⁴⁰ IHCA Section 6 A.

²⁴¹ IHCA Section 7 A.

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| | recipient authority being subject to adequate confidentiality requirements and safeguards that are appropriate to the nature and sensitivity of the information to be disclosed. |
| Description and findings re EC12.2 | <p>DFA and Banking.²⁴² The FBAs are authorized, at their discretion, to furnish any report of examination or other confidential supervisory information concerning any IDI or other entity examined by such agency to any other federal or state agency or authority with supervisory or regulatory authority over the IDI or other entity, and to any other person that the FBA determines to be appropriate.²⁴³ The latter reference may thus entail disclosure of information to foreign authorities. In addition, the five supervisory agencies that comprise the Federal Financial Institutions Examination Council,²⁴⁴ the SEC, the Federal Trade Commission, the CFTC and the CFPB are authorized to exchange financial records, examination reports and other information with respect to a financial institution, holding company or any subsidiary of an IDI or holding company.²⁴⁵</p> <p>In addition, the FBAs have statutory authority to disclose information obtained in the course of exercising their supervisory or examination authority to any foreign bank regulatory or supervisory authority, provided that the disclosure is appropriate and does not prejudice the interests of the U.S.²⁴⁶ The U.S. authorities interpret the latter safeguard with broad discretion.</p> <p>The FDIC, as receiver for an IDI and for the purposes of carrying out its powers, may provide assistance to any foreign banking authority.²⁴⁷</p> <p>Each of the FBAs has promulgated regulations governing the disclosure of non-public information.²⁴⁸ These regulations generally require that the applicable FBAs, prior to disclosing confidential information, obtain assurances that the information disclosed will be kept confidential.</p> <p>The FBAs have entered into a number of memoranda of understanding, statements of cooperation, and other arrangements establishing frameworks for cooperation and the exchange of information in connection with their respective supervisory, resolution, and other responsibilities with foreign authorities. These memoranda of understanding and statements of cooperation contain a number of conditions to govern the confidentiality of information (e.g., restricting usage to lawful supervisory purposes while holding information confidential; requesting prior consent before sharing with third parties; reacting to disclosures required by statute or legal process).</p> <p>The FBAs are, however, authorized to share relevant supervisory information with foreign authorities even in the absence of a formal arrangement such as a memorandum of</p> |

²⁴² The analysis of EC 12.2, 12.3 and 12.4 is of a general nature as it pertains to the legal gateways for the disclosure of non-public information. No distinction is therefore made between the description and findings under DFA and the FDI Act.

²⁴³ FDI Act, 12 USC. § 1817(a)(2)(C).

²⁴⁴ The Federal Financial Institutions Examination Council comprises the OCC, the FDIC, the Federal Reserve Board, the Consumer Financial Protection Bureau, the National Credit Union Administration Board, and the State Liaison Committee. See 12 USC. § 3303(a).

²⁴⁵ 12 USC. § 3412(e).

²⁴⁶ 12 USC. § 3109(a).

²⁴⁷ FDI Act, 12 USC. § 1818(v) and 1821 (r).

²⁴⁸ 12 C.F.R. Part 4 (OCC); 12 C.F.R. § 211.27 and 12 C.F.R. Part 261 (Federal Reserve Board); 12 C.F.R. § 309.6 and 12 C.F.R. § 347.207 (FDIC); and 12 C.F.R. Part 1070 (CFPB).

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| | <p>understanding.</p> <p>While the above mentioned statutory provisions refer to the sharing of information of a broad supervisory nature, the U.S. authorities interpret them in a manner that encompasses also resolution-related information, based on a number of grounds. First, supervisory information is relevant also in a resolution context. Second, the statutes do not distinguish as to whether the information is obtained by the FBAs in a supervisory rather than in a resolution capacity, and therefore do not pose limitations on the sharing of such information in a resolution context. In practice, FBAs share significant information with authorities playing a role in resolution in both a home and host capacity.</p> <p>State Insurance. State insurance holding company legislation generally provides the state commissioner with broad authority to share, in normal times and in a crisis, non-public information necessary for recovery and resolution planning and for carrying out resolution, to relevant domestic and foreign authorities as well as ancillary supervisory authorities.</p> <p>For example, Section 8 C (1) of IHCA authorizes the commissioner, as regulator, to share documents, materials or other information including confidential and privileged documents, materials or information with other state, federal and international regulatory agencies, with NAIC and its affiliates and subsidiaries, and with state, federal, and international law enforcement authorities (including members of supervisory colleges), provided that the recipient agrees in writing to maintain the confidentiality and privileged status of such information and has verified in writing the legal authority to maintain confidentiality.</p> <p>Findings. The U.S. regime contains adequate legal gateways for the disclosure of non-public information for recovery and resolution planning and for carrying out resolution to domestic and foreign authorities. The statutory interpretation given by the U.S. authorities, allowing the possible disclosure of resolution-related information under the existing legal framework, is reinforced by their practice of sharing information with foreign resolution authorities, subject to certain safeguards and confidentiality requirements. Similar conclusions apply with respect to the state insurance resolution regime.</p> <p>For the sake of clarity, consideration may be given to updating the relevant statutes so as to explicitly mention the sharing of resolution-related information.</p> |
| EC12.3 | <p>The legal framework or resolution regime incorporates adequate safeguards to protect the confidentiality of non-public information received from other domestic or foreign authorities. Such safeguards:</p> <ul style="list-style-type: none"> (i) require authorities to keep such information confidential and to use it only in accordance with the terms on which the information was provided; (ii) prohibit domestic authorities from disclosing such information to other domestic or foreign authorities or other third parties without the prior express consent of the authority that provided it, unless such disclosure is compelled by law; and (iii) exclude information received from foreign authorities from mandatory disclosure pursuant to freedom of information or similar legislation that may exist in that jurisdiction, or treat such information as falling under an exemption from disclosure requirements. |
| Description and findings | <p>DFA and Banking. FBAs are prohibited from disclosing certain types of confidential financial information unless such sharing is specifically authorized by law.²⁴⁹ As noted under EC 12.2</p> |

²⁴⁹ 18 USC. § 1905.

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| re EC12.3 | <p>above, each of the FBAs has promulgated regulations governing the disclosure of non-public information, setting forth certain confidentiality requirements.</p> <p>The FBAs may deny demands for non-public information in their possession, including non-public information received from domestic or foreign authorities, except in limited situations in which they are legally compelled to disclose otherwise non-public information pursuant to a subpoena or court order. Non-public information may be subpoenaed by a court, a grand jury, or a committee of Congress. If a FBA receives a subpoena from a litigant, a government agency or Congress and declines to produce the non-public information, the party that obtained the subpoena may go to court and enforce it. If a FBA declines to release the information requested by the litigant or others, the requester may file an action under the Administrative Procedure Act,²⁵⁰ in which case the FBA's decision may be reviewed to determine whether it is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." When feasible, a FBA that is being compelled to provide non-public information received from another domestic or foreign authority will notify such authority and make reasonable efforts to resist disclosure.</p> <p>By statute, the sharing of any information between federal agencies that is deemed privileged shall not be deemed a waiver of any privilege applicable to that information.²⁵¹ In addition, an FBA that obtains protected or confidential information from another FBA may not share that information with another regulatory authority without first obtaining prior written permission from the FBA that provided the information.²⁵² Under the IBA, non-public information provided by a foreign authority to a FBA will have broad protection from compelled onward disclosure where, among other things, the non-public information is obtained pursuant to a memorandum of understanding or similar arrangement, and where the foreign authority has made a written representation to the FBA that public disclosure of the information would violate the laws applicable to the foreign authority.²⁵³ If these statutory requirements are satisfied, a FBA cannot be compelled to disclose such information except to duly authorized committees of Congress or to comply with a validly issued order of a court of the U.S.</p> <p>This statutory protection from disclosure constitutes a statute within the meaning of the Freedom of Information Act, which provides that information specifically exempted from disclosure by statute may not be disclosed.²⁵⁴</p> <p>Even in the absence of the IBA's protections, information received from foreign authorities could be exempt from disclosure under two of the other exemptions to disclosure contained in the Freedom of Information Act. One exemption protects "trade secrets and commercial or financial information obtained from a person [that is] privileged and confidential." The term "person" has been construed to include agencies of foreign governments.²⁵⁵ Another exemption protects matters that are contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions. According to the U.S. authorities, the protection given under this exemption for examination-related information would likely extend to any such material that the</p> |
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²⁵⁰ 5 USC. § 701 *et seq.*

²⁵¹ FDI Act, 12 U.S.C. § 1821(t).

²⁵² 12 CFR § 261.20(g), 12 CFR § 4.36(d) and 4.37(c) and (d).

²⁵³ 12 USC. § 3109(c)(1).

²⁵⁴ 5 USC. § 552(b)(3)

²⁵⁵ See United States Department of Justice, *Guide to the Freedom of Information Act* (2009 ed.) at 271, n. 45.

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| | <p>FBA received from a foreign authority.</p> <p>State Insurance. State insurance holding company legislation generally establishes broad safeguards to protect the confidentiality of non-public information received from other domestic or foreign authorities.</p> <p>For example, Section 8A of IHCA designates the documents, materials and other information in possession or control of the regulatory authority that have been received from other authorities in connection with group-wide supervision (which includes information obtained in regard to a supervisory college or through his crisis management tasks) as confidential by law and privileged. The IHCA expressly excludes such information from disclosure through freedom of information legislation, subpoena or discovery, or from admission in evidence in any private civil action. The commissioner may share confidential and privileged information with other states, federal and international regulatory agencies, with NAIC and its affiliates and subsidiaries, and with state, federal, and international law enforcement authorities if the recipients agrees in writing to maintain confidentiality and privileged status of the information, and has verified in writing the legal authority to maintain confidentiality (as discussed in EC12.2).</p> <p>The commissioner may receive confidential and privileged information from the NAIC and its affiliates and subsidiaries and from regulatory and law enforcement officials of other foreign or domestic jurisdictions, provided that such information received must be maintained as confidential or privileged.²⁵⁶</p> <p>Findings. The U.S. legal framework contains adequate safeguards to protect the confidentiality of non-public information received from other domestic or foreign authorities.</p> |
| <p>EC12.4</p> | <p>The resolution authority has policies and procedures in place to control and monitor the dissemination within the authority of non-public information received from a foreign home or host authority.</p> |
| <p>Description and findings re EC12.4</p> | <p>DFA and Banking. The FDIC policy is to use non-public information received from foreign authorities only in accordance with the terms on which it was provided. Under FDIC internal rules, the authority to establish policies and procedures is delegated to the heads of relevant divisions, such as the director of the RMS Division and of the Division of Resolutions & Receiverships. Policies and procedures may include, in the first instance, making such non-public information available to relevant staff on a need-to-know basis. The FDIC has also instituted procedures designed to limit access to non-public information to specific employees. These procedures include the use of computer software platforms to serve as secure repositories for non-public information to which only specific staff may be granted access by a limited number of authorized officials, where such access is routinely monitored. With respect to physical copies of non-public information, these procedures include the use of designated rooms and storage facilities access to which is restricted to authorized staff.</p> <p>State Insurance. There are policies and procedures in force that regulate the treatment of sensitive information from foreign authorities. The employees of the commissioner are subject to state law provisions that prohibit the divulgement of confidential information obtained in the performance of their duties. Additionally, the NAIC-sponsored Master Information-Sharing and Confidentiality Agreement (MISCA) intends to secure a proper standard for the confidentiality of supervisory related information on insurance companies. According to MISCA, the commissioners have to follow standards on the control of internal dissemination of confidential</p> |

²⁵⁶ IHCA Section 8C(3).

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| | <p>information received from a foreign authority.</p> <p>Findings. The FDIC and the state authorities have policies and procedures in place to control and monitor the dissemination within the authority of non-public information received from a foreign home or host authority.</p> |
| EC12.5 | <p>Firms subject to a recovery and resolution planning requirement are required to maintain management information systems that are capable of producing information necessary for recovery and resolution planning, assessing resolvability and the conduct of resolution, including the items specified in KA 12.2, and delivering that information to the authorities on a timely basis.</p> |
| Description and findings re EC12.5 | <p>DFA. Firms subject to recovery and resolution planning requirements are expected to ensure that, among others, recovery planning capabilities are sufficiently integrated into their corporate governance structures and processes, and effectively supported by robust MIS (also see EC11. 4).</p> <p>The FRB has issued detailed guidance, on the capabilities that firms should have in place support effective recovery or resolution preparedness.²⁵⁷ As per the relevant supervisory guidance, firms are expected to have, at minimum:</p> <ul style="list-style-type: none"> (i) effective processes for managing, identifying, and valuing collateral it receives from and posts to external parties and affiliates; (ii) a comprehensive understanding of obligations and exposures associated with payment, clearing, and settlement activities; (iii) the ability to analyze funding sources, uses, and risks of each material entity and critical operation, including how these entities and operations may be affected under stress; (iv) demonstrated MIS capabilities for producing certain key data on a legal entity basis that is readily retrievable and controls in place to ensure data integrity and reliability; and (v) and robust arrangements for the continued provision of shared or outsourced services needed to maintain critical operations that are documented and supported by legal and operational frameworks. <p>The ability to demonstrate adequate MIS capabilities is covered in more detail in the Principles and Practices for Recovery and Resolution Preparedness that have been issued by the FRB in January 2014.²⁵⁸ According to these Principles, which are broadly in line with FSB guidance, G-SIBs should be able to timely produce,</p> <ul style="list-style-type: none"> (i) monthly financial statements for each material entity; (at least monthly); (ii) external and intragroup credit exposures (on- and off-balance sheet, by type of exposure, counterparty, maturity, and gross payable and receivable); (iii) gross and net risk positions with internal and external counterparties; |

²⁵⁷ Heightened Supervisory Expectations for Recovery and Resolution Preparedness for Certain Large Bank Holding Companies (SR 14-1).

²⁵⁸ Principles and Practices for Recovery and Resolution Preparedness, <http://www.federalreserve.gov/bankinfo/srletters/sr1401a1.pdf>.

- (iv) guarantees, cross holdings, financial commitments and other transactions between material entities; data to facilitate third-party valuation of assets and businesses, including risk metrics; key third party contracts, including the provider, provider's location, service(s) provided, legal entities that are a party to or a beneficiary of the contract, and key contractual rights (for example, termination and change in control clauses);
- (v) legal agreement information, including parties to the agreement and key terms and interdependencies (for example, change in control, collateralization, governing law, termination events, guarantees, and cross-default provisions);
- (vi) service level agreements between affiliates, including the service(s) provided, the legal entity providing the service, legal entities receiving the service, and any termination/transferability provisions;
- (vii) licenses and memberships to all exchanges and value transfer networks, including FMUs; key management and support personnel, including dual hatted employees, and any associated retention agreements;
- (viii) agreements and other legal documents related to property, including facilities, technology systems, software, and intellectual property rights; and
- (ix) updated legal records for domestic and foreign entities, including entity type and purpose (for example, holding company, bank, broker-dealer, and service entity), jurisdiction(s), ownership, and regulator(s).

Observance of the aforementioned guidance is being tested as part of ongoing supervisory activities.

In 2014, the FRB launched a comprehensive review of the recovery and resolution preparedness of the eight U.S.-based G-SIBs. The review covers, among others, the capabilities of firms' management information systems for producing relevant data in a timely and reliable fashion.

Banking. Pursuant to the FDIC's IDI Rule, covered IDIs are required to include in their plans a detailed inventory and description of key management information systems and applications for risk management, accounting, and financial and regulatory reporting. In particular, firms are required to identify the legal owner or licensor of the systems; describe their use and functions; provide a listing of service level agreements, as well as software and systems licenses; and describe the capabilities of the firms' processes and systems to collect, maintain, and report the information and other data underlying the plan to the firms' senior management and, upon request, the FDIC. Any deficiencies in such capabilities should be identified, together with actions the firm intends to take to promptly address these. Implementation timelines should also be specified.²⁵⁹

In addition, firms are required to provide a mapping of critical services—which may include management information systems and applications that are critical for the orderly operation of the firm—to material entities and core business units.

In its public guidance for the IDI resolution plans under the FDI Act, released in December 2014, the FDIC calls attention to five significant obstacles to an orderly and least costly resolution, as identified during the FDIC's internal resolution plan review process.²⁶⁰ Loss of access to relevant

²⁵⁹ 12 CFR § 360.10 (c)(2)(xix).

²⁶⁰ <https://www.fdic.gov/news/news/press/2014/pr14109.html>

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| | <p>data, management information systems and IT—resulting in the inability to generate timely and accurate reporting—is flagged as one of the five key obstacles that covered IDIs are required to discuss in their plans. Where necessary, such discussion needs to be supplemented with mitigating actions or steps that the firms intends to take, together with a timeline for the implementation thereof.</p> <p>State Insurance. There are no particular provisions in state law that require insurance companies to maintain management information systems for producing information that is especially necessary for recovery and resolution planning.</p> <p>Based on NAIC model legislation, states have enacted provisions for the production of certain information on the financial conditions of the insurance companies but there is no specific focus on recovery and resolution planning. Nevertheless, setting up systems for sound and comprehensive information support on the financial status of the company for the board members and establishing a high-level risk committee as well as risk officers in each entity or line of business is widely recognized as an important standard in financial sector supervision.</p> <p>Findings. Firms subject to resolution planning are required to demonstrate MIS capabilities for producing, on a legal entity basis, data that is relevant for recovery and resolution planning, for assessing resolvability and for the conduct of resolution. State insurance resolution regimes do not have provisions requiring the maintenance of MISs for recovery and resolution planning purposes.</p> |
| <p>EC12.6</p> | <p>The jurisdiction has in place processes (for example) through regular examinations to test the firms’ capability to produce information for recovery and resolution planning and in resolution quickly.</p> |
| <p>Description and findings re EC12.6</p> | <p>DFA. The authorities have an array of tools and techniques to carry out their supervisory responsibilities especially with regard to the banking sector.²⁶¹ The supervisory process, which has a strong risk-based focus, is robust, with a high proportion of mandated reviews (both offsite and onsite), a uniform rating process and an extensive planning process that agrees the supervisory strategy going forward. U.S. regulators have a statutory responsibility to ensure and evaluate safety and soundness and are continuously improving existing—and developing new—methodologies and techniques, such as stress testing and horizontal reviews.</p> <p>The FBAs have implemented an enterprise-wide supervisory approach that cuts across legal entities. In carrying out this approach, the agencies evaluate the effectiveness of the firm’s policies, procedures, controls, management information systems and risk management processes across the organization. The evaluation of key corporate governance functions and primary firm-wide risk management and internal control functions includes cross-border operations.</p> <p>Supervisory objectives are accomplished through a combination of on-site examinations and off-site surveillance. In general, the primary FBA conducts annual, on-site examinations of the banks within its jurisdiction. Through on-site examinations and continuous supervision, supervisory staff generally:</p> <ul style="list-style-type: none"> (i) evaluate the soundness of the bank’s or holding company’s assets and the effectiveness of its internal controls, policies, and management; (ii) analyze key financial factors such as the bank’s and holding company’s capital, earnings, |

²⁶¹ Also see the conclusions of the detailed assessment of observance of the Basel Core Principles for Effective Banking Supervision.

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| | <p>liquidity, and sensitivity to interest rate risk;</p> <p>(iii) assess the bank’s or holding company’s exposure to off-balance-sheet risks;</p> <p>(iv) check for compliance with banking laws and regulations; and</p> <p>(v) determine the bank’s or holding company’s overall soundness and solvency.</p> <p>Off-site supervision involves monitoring and assessment of information from a variety of sources, including standard regulatory reports and internal information received from the supervised bank and holding company. The standard regulatory reports capture a host of commercial and financial information on supervised entities. Off-site surveillance also includes a review of reports of recent examinations and inspections, internal management and internal and external auditor reports (which may relate to firms’ MIS capabilities).</p> <p>Banking. In general, IDIs are to be subjected to a full-scope, on-site examination on an annual basis, which are typically conducted by the FBA that is primarily responsible for the relevant institution.²⁶² To minimize the disruptive effects of examinations of the operations of IDIs, such examinations are to be coordinated with the other FBA and the appropriate state supervisor(s) and shall take account of examination reports prepared by any other FBA. As highlighted above, the examinations cover, among other things, the effectiveness of the IDIs’ MIS and risk management processes across the organization.</p> <p>In addition to such recurrent examinations, the IDI Rule explicitly prescribes that covered IDIs provide the FDIC with all information that the FDIC deems necessary to assess both the resolution plan’s credibility and the covered IDI’s ability to implement said plan. In a similar vein, covered IDIs are required to demonstrate their capability to produce promptly—in a timeframe and format acceptable to the FDIC—the information and data underpinning the resolution plan. This provides the FDIC with another process for testing covered IDIs’ MIS capabilities.²⁶³</p> <p>Finally, the FDI Act provides the FDIC with the authority to conduct special examinations of IDIs whenever its Board of Directors determines that such an examination is necessary to determine the condition of the institution for insurance purposes, as discussed under EC 12.1.</p> <p>State Insurance. There are no explicit provisions in state law that require procedures for testing the firms’ ability to timely produce information that is relevant for recovery and resolution planning, as specific standards on resolution preparedness and capabilities are lacking (also see EC 12.5). However, state commissioners have the power under state law to undertake on-site inspections at any time without prior notice. They are permitted to request any information on financial conditions of the insurance companies, but as there is no specific requirement for recovery and resolution planning under state law, it is not clear to what extent such testing can be meaningful.</p> <p>Findings. Firms’ capabilities to promptly produce any and all information that may be necessary for recovery and resolution planning purposes, as well as in resolution scenarios, are periodically being tested via recurrent supervisory activities.</p> |
| Assessment of KA12 | |
| Comments | The U.S. bank and insurance resolution regimes provide for adequate powers enabling the authorities to have access and to share of information that is material for the planning, preparation and implementation of resolution measures. |

²⁶² FDI Act 12 USC. § 1820 (d), with the *caveat* that the FDIA provides for an extension of the examination cycle to once every 18 months to smaller institutions (total assets of less than US\$500 million) that are well capitalized, well managed and otherwise not subject to a formal enforcement proceeding or order.

²⁶³ 12 CFR § 360.10(d).

RECOMMENDED ACTIONS AND AUTHORITIES

COMMENTS

A. Summary of Recommended Actions

| Reference Principle | Recommended Action |
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| KA1 | <ul style="list-style-type: none"> Extend the scope of OLA powers to systemically important insurance companies and U.S. branches of foreign banks. |
| KA2 | <ul style="list-style-type: none"> Finalize the procedural rules detailing the interaction between the various federal authorities in relation to the commencement of a Title II proceeding under the “three key process”. Pending implementation of the recommendation in KA 1, clarify the roles and responsibilities between federal and state authorities in the resolution of an insurance group under Title II, including with respect to the triggers, objectives, coordination mechanisms and funding sources. |
| KA3 | <ul style="list-style-type: none"> Issue guidance on the circumstances (e.g., with scenarios) under which OLA may commence prior to insolvency, with specific examples and which clearly aligns with non-viability. Adopt powers in the FDI Act to recover compensation, including variable remuneration, from those “substantially responsible” for the failure of the firm. Adopt powers under DFA and FDI Act and in state insurance law to require companies in the same group (whether or not they are regulated or are themselves subject to a bankruptcy or resolution proceeding) to continue to provide services, including those not governed by contract, as necessary to support effective resolution. Issue a final notice or regulation, clarifying in further detail, key aspects of the SPE approach including with regard to the valuation process, the communication strategy, and the legal mechanics for establishing a new holding company, the treatment of creditors who would not meet the suitability requirements for shareholders, the disclosure and registration requirements and related waivers applying in a Title II proceeding. |
| KA4 | <ul style="list-style-type: none"> Amend the FDI Act to provide the power to override early termination rights in contracts of subsidiaries and affiliates of an IDI. |
| KA5 | <ul style="list-style-type: none"> Identify the disclosure requirements that, in the context of a Title II liquidation, may warrant a temporary and limited waiver, and adopt relevant regulatory changes. |
| KA6 | <ul style="list-style-type: none"> Pending implementation of recommendation in KA 1, clarify whether there are any circumstances in which the OLF could be used in connection with the resolution of an insurance company under state insurance resolution laws (e.g., with the FDIC appointed as receiver). |

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| KA7 | <ul style="list-style-type: none"> • Introduce statutory mechanisms to give prompt legal effect in the United States to actions taken by foreign resolution authorities, either by recognition or by taking supportive measures of such actions respecting banks. • Introduce a requirement under the FDI Act for the FDIC, as resolution authority, to cooperate with foreign resolution authorities by taking into account the impact of the resolution measure taken by the FDIC on financial stability in the relevant jurisdictions. • Amend the bank and insurance resolution regimes to require the authorities involved in the resolution of a U.S. branch (e.g., OCC, Superintendent), to cooperate with a foreign resolution authority. • Introduce a requirement under the bank and insurance resolution regimes to notify and consult with the home resolution authority of a foreign firm prior to exercising resolution powers in relation to a local subsidiary or branch of such firm. • Extend the depositor preference rule to depositors of U.S. branches in foreign jurisdictions, whether or not the deposits are payable in the United States. |
| KA8 | <ul style="list-style-type: none"> • Formalize criteria for determining the membership of CMGs. • Align the engagement with host authorities that are not represented on CMGs with relevant FSB guidance. |
| KA9 | <ul style="list-style-type: none"> • Finalize COAGs for all U.S.-based G-SIIs. |
| KA10 | <ul style="list-style-type: none"> • Finalize resolvability assessments for all domestic systemically important firms, where appropriate in cooperation with relevant host authorities. • Provide the agencies with explicit powers to require changes to IDIs' business practices, legal, operational or financial structures that are deemed necessary to improve their resolvability. |
| KA11 | <ul style="list-style-type: none"> • Develop specific guidance for recovery and resolution planning for systemic insurance groups (e.g., on issues such as the identification of critical functions, the appropriate capital structure for an insurance group, and the development of appropriate resolution strategies) and progress reforms necessary to enhance resolvability. • Continue to pursue reforms to enhance resolvability, including under Title II, and where necessary invoke regulatory authority to require firms to address identified deficiencies (also see KA10). • Provide the agencies with the authority to require recovery and resolution plans from BHCs and IDIs (irrespective of asset size) in situations where other characteristics (for example in view of their interconnectedness, substitutability and complexity) suggest that they could nonetheless be systemically significant or critical at the point of failure. |
| KA12 | None |

Appendix I. Resolution Legislation Applicable to Different Financial Firms

| Sector | Type | Sub-type (if relevant) | Primary regulator | Resolution Authority | Resolution Funds | Resolution Legislation | If Title II systemic risk determination made | | | |
|------------------------------------|---|---|-------------------------|---|----------------------------|--|--|--------------------------------------|----------------------------|-------------------|
| | | | | | | | Resolution Authority | Resolution Funding | Resolution Legislation | |
| Holding companies & group entities | Large bank holding companies (BHCs) | | Federal Reserve | Court appointed trustee | None | Chapter 7 or 11 of the bankruptcy code | FDIC | OLF | DFA | |
| | Financial holding companies (FHCs) which meet enhanced regulatory standards | | | | | | | | | |
| | Savings & loans holding companies (SLHC) which meet enhanced regulatory standards | | | | | | | | | |
| | Intermediate Holding Companies (IHC) ¹ | | | | | | | | | |
| | Nonbank subsidiaries ² of large BHCs, FHCs, SLHCs, IHCs | Non-insurance/non broker-dealer, regulated subsidiaries | | Federal Reserve or functional regulator | Court appointed trustee | None | Chapter 7 or 11 of bankruptcy code | FDIC ³ | OLF | DFA |
| | | Non-regulated subsidiaries | | None | Court appointed trustee | None | Chapter 7 or 11 of bankruptcy code | | | |
| | | Insurance company subsidiaries | | State regulator | State resolution authority | State guaranty association | State legislation | State regulator or FDIC ⁴ | State guaranty association | State legislation |
| Broker dealer subsidiaries | | SEC | Court appointed trustee | SIPC | SIPA | FDIC ³ /SIPC ⁵ | SIPC/OLF ⁶ | SIPA/ DFA ⁷ | | |

¹ FBOs with non-branch/ non-agency US assets of \$50 billion or above are required to establish a US based IHCs by 1 July 2016, as the US parent of all their US bank and non-bank subsidiaries (e.g., broker-dealers, finance companies, and special purposes entities) but not branch assets and liabilities.

² Nonbank subsidiaries engaged in securities, commodities or insurance activities are supervised by their functional regulators e.g., broker-dealer, investment adviser, investment company regulated by the SEC; an insurance company or insurance agent subject to supervision by a state regulator; and a nonbank subsidiary engaged in CFTC regulated activities.

³ For subsidiaries deemed "covered subsidiaries" or "covered broker-dealers" including those predominantly engaged in activities that are financial in nature or incidental thereto.

⁴ Title II of the DFA provides that a systemically important insurance company (as opposed to the parent company of the insurance company) is to be resolved pursuant to state law. If the appropriate state authority does not commence the resolution of the insurance company within 60 days of a systemic risk determination by the Treasury Secretary, then the FDIC shall have the authority to stand in the place of the appropriate regulatory agency and file the appropriate judicial action in the appropriate state court to place such company into orderly liquidation under the laws and requirements of the state (not the OLA powers).

⁵ The SIPC acts as trustee for the covered broker or dealer in the Title II resolution of covered broker-dealers.

⁶ Under Sec. 205 (e) (2) of the DFA, SIPC satisfies customers' claims in the manner and amount provided under SIPA. FDIC satisfies customers' claims to the extent that a customer would have received more securities or cash with respect to the allocation of customer property had the covered financial company been subject to a proceeding under SIPA.

⁷ Except as otherwise provided in Section 205 of DFA, SIPA administers the determination of claims and the liquidation of assets retained in the receivership of the covered broker or dealer and not transferred to a bridge financial company.

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| Non-bank SIFIs designated by FSOC under Title I of the DFA (Sec.113) for FRB supervision ⁸ | FSOC designated non-banks SIFIs that are not insurance companies | | Federal Reserve | Court appointed trustee | None | Chapter 7 or 11 of bankruptcy code |
| | FSOC designated SIFIs that are insurance companies | | | State resolution | State guaranty association | State legislation |
| Insurance companies not designated as SIFIs under Title I (Sec.113) | | | State regulator | State resolution authority | State guaranty association | State legislation |
| Broker dealers not designated as SIFIs under Title I (Sec.113) | | | SEC | Court appointed trustee | SIPC | SIPA |
| Deposit-takers | National banks | | OCC | FDIC | DIF | FDIA |
| | State banks | Member Federal Reserve | Federal Reserve | | | |
| | | Nonmember Federal Reserve | FDIC | | | |
| | Savings and loan associations | State-licensed | FDIC | | | |
| | | Federally licensed | OCC | | | |
| | Subsidiaries, branches & agencies of foreign bank organizations (FBOs) without FDIC coverage | State-licensed | Federal reserve or state regulator ⁹ | State resolution authority or OCC appointed receiver ¹⁰ | None | State legislation or International Banking Act |
| | | Federally licensed | OCC | OCC appointed receiver | None | International Banking Act of 1978 |
| | FBOs with grandfathered FDIC coverage ¹¹ | State-licensed | FDIC | FDIC | DIF | FDIA |
| | | Federally licensed | OCC | | | |
| | Credit unions | State-licensed | State regulator | NCUA | NCUSIF ¹² | FCUA |
| Federally licensed or state licensed which elect for a Federal regulator | | NCUA | | | | |

| | | |
|--------------------------------------|----------------------------|------------------------|
| FDIC | OLF | DFA |
| State regulator or FDIC ⁴ | State guaranty association | State legislation |
| State regulator or FDIC ⁴ | State guaranty association | State legislation |
| FDIC ³ /SIPC ⁵ | SIPC/OLF ⁶ | SIPA/ DFA ⁷ |

⁸ The FSOC has designated four nonbank financial companies—AIG, General Electric Capital Corporation, Metlife and Prudential Financial, Inc.—and eight financial market utilities (FMUs) to date.

⁹ On a joint or alternate (i.e. rotating) basis.

¹⁰ Where a FBO has one or more state licensed branches and one or more federally licensed branches, and the OCC appoints a receiver for the Federal branch or agency, the receiver shall take possession of all the property and assets of such FBO in the United States, not only the property and assets of the Federal branch. See 12 U.S.C. § 3102(j).

¹¹ As of December 19, 1991, FBOs may not establish insured branches in the United States. However, insured branches operating as of that date were permitted to continue operating. There are currently ten insured branches in the United States.

¹² Unless opted out of NCUSIF scheme.