

The Meeting of the Systemic Resolution Advisory Committee

of the

Federal Deposit Insurance Corporation

Federal Deposit Insurance Corporation Building

Washington, D.C.

Open to Public Observation Via Webcast

November 9, 2022 - 9:00 A.M.

The meeting of the FDIC Systemic Resolution Advisory Committee (Committee) was called to order by Martin J. Gruenberg, Acting Chairman of the Board of Directors, Federal Deposit Insurance Corporation (FDIC or Corporation).

Committee Members present in person at the meeting:  
Tim P. Clark, Distinguished Senior Banking Advisor, Better Markets (nonprofit organization) and Former Deputy Director, Division of Supervision and Regulation, Federal Reserve Board of Governors; Jay Clayton, Senior Policy Advisor and Of Counsel, Sullivan & Cromwell LLP and Former Chairman, U.S. Securities and Exchange Commission (SEC); H. Rodgin Cohen, Senior Chair, Sullivan & Cromwell LLP; Gary Cohn, Vice Chairman, IBM, Former Director, U.S. National Economic Council, Former Assistant to the President for Economic Policy and Former President and Chief Operating Officer, The Goldman Sachs Group, Inc.; Honorable Robert Drain, United States Bankruptcy Judge, Southern District of New York; D. Wilson Ervin, Former Vice Chairman and Global Chief Risk Officer, Credit Suisse; Richard J. Herring, Founding Co-Director, The Wharton Financial Institutions Center, Jacob Safra Professor of International Banking and Professor of Finance, The Wharton School, University of Pennsylvania; Donald Kohn, Former Vice Chairman, Board of Governors of the Federal Reserve System and Senior Fellow, Economic Studies Program, Brookings Institution; Frank La Salla, President and Chief Executive Officer and Director, Depository Trust & Clearing Corporation (DTCC), and President and Chief Executive Officer of DTCC's principal subsidiaries Depository Trust Company (DTC), Fixed Income Clearing Corporation (FICC) and National Securities Clearing Corporation (NSCC); Timothy J. Mayopoulos, President of Blend (NYSE-listed cloud-based software company), Former President and Chief Executive Officer of Fannie Mae and Former

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General Counsel of Bank of America; Sandie O'Connor, Financial Industry Expert and Former Chief Regulatory Affairs Officer, JPMorgan Chase; Douglas L. Peterson, President and Chief Executive Officer and Board Member, S&P Global and Former Chief Operating Officer, Citibank, N.A.; John S. Reed, Former Chairman and CEO of Citigroup, Former Chairman of the New York Stock Exchange and Former Chairman, Corporation of Massachusetts Institute of Technology (MIT); and Margaret (Meg) E. Tahyar, Partner and Co-Head of Financial Institutions, Davis Polk LLP.

Committee Members attending by video conference: Sheila Bair, Former Chairperson, Federal Deposit Insurance Corporation; and Honorable Shelley C. Chapman, Senior Counsel, Willkie Farr & Gallagher LLP and Former United States Bankruptcy Judge, Southern District of New York.

Committee Member Dr. Ben S. Bernanke, Distinguished Fellow in Residence with the Economic Studies Program at the Brookings Institution and Former Chairman of the Board of Governors of the Federal Reserve System, was absent from the meeting.

Members of the Corporation's Board of Directors present at the meeting: Martin J. Gruenberg, Acting Chairman; Rohit Chopra, Director (Director, Consumer Financial Protection Bureau); and Michael J. Hsu, Director (Acting Comptroller of the Currency).

Corporation staff in attendance at the meeting: Susan L. Baker, Tawanta L. Brinson, Shaheerah M. Carmichael, Mary Calkins, John P. Conneely, Kymberly K. Copa, Laura C. Crawford, Jermain Cunningham, BalKrishna N. Dave, Angela Dean, Debra A. Decker, Samantha G. Ekholm, Gerald M. Evans, Elizabeth Falloon, Andrew J. Felton, Sheila R. Finlayson, Joanne Fungaroli, Gregory Gelzinis, Michelle G. Gilbert, Patricia S. Gurneau, Sheridan L. Hill, Krista Hughes, Kete M. Iluyomade, Veronique R. James, Rosilyn L. King, James L. McGraw, Arthur J. Murton, Nikita Pearson, Harrel M. Pettway, Jerrod Sanders, Alfred L. Seivold, James P. Sheesley, Richard Penfield (Pen) Starke, Nicole J. Tettegah, Ryan P. Tetrick, Mona L. Thomas, Jenny G. Traille, David Wall, Aaron W. Wishart, and Allen Yarbrough.

Other guests in attendance: Elke Koenig, Chair, Single Resolution Board, European Union; and Jon Cunliffe, Deputy Governor for Financial Stability, Bank of England (attended via video conference).

## Welcome and Introduction

Acting Chairman Gruenberg presided over the proceeding. He began by welcoming everyone to the in-person meeting, noting that it had been two years since the last meeting which was held virtually in October of 2020 due to the pandemic and four years since the Committee had actually met in person. He shared his intention to resume the regular annual meeting schedule for the Committee, further pointing out the important role the Committee plays in helping FDIC work through the challenges involving systemic resolution and the value in meeting in-person more regularly to receive the Committee's input on the work FDIC is undertaking.

Acting Chairman Gruenberg introduced the five new members of the Committee: Timothy (Tim) Clark - Distinguished Senior Banking Advisor of Better Markets and Former Deputy Director of Supervision and Regulation at the Federal Reserve Board of Governors; Frank La Salla - President and Chief Executive Officer of the Depository Trust & Clearing Corporation (DTCC); Jay Clayton - Former Chairman of the SEC; Margaret (Meg) Tahyar - Partner and Co-Head of Financial Institutions at Davis Polk LLP; and D. Wilson Ervin, Former Vice Chairman at Credit Suisse.

Acting Chairman Gruenberg also introduced Elke Koenig - Founding Chair of the Single Resolution Board for Europe, who was attending the meeting as a special guest. He said that Ms. Koenig's service on the Single Resolution Board (SRB) would be ending next month due to term limits and that she has agreed to join the Committee upon her term end.

The Acting Chairman then recognized the four former members of the Committee who had cycled off the Committee since the last meeting: William (Bill) Donaldson (former Chairman of the SEC); Peter Fisher (former Undersecretary of the Treasury and Senior Fellow of the Center for Global Business and Government at the Tuck School of Business at Dartmouth University); Gary Stern (former CEO and President of the Federal Reserve Bank of Minneapolis); and Michael Bodson (former President and CEO of the DTCC).

Acting Chairman Gruenberg concluded his welcoming remarks by providing an overview of the session topics for the meeting.

The Acting Chairman thanked and welcomed back the returning members of the Committee, and recognized FDIC Board Members Michael Hsu and Rohit Chopra, who were also in attendance. Both

Directors Hsu and Chopra made welcoming remarks.

The Acting Chairman then turned the program over to John Conneely, Director of the Division of Complex Institution Supervision and Resolution (CISR), to moderate the proceeding. Mr. Conneely reviewed the agenda and made a statement regarding the Sunshine Act, confirming that this was not a meeting to conduct business of the FDIC Board of Directors and that the Board members present would only engage in general or preliminary discussions that do not relate to specific proposals for action pending before the FDIC. He also made an announcement regarding a recently-issued advanced notice of proposed rulemaking (ANPR) that was jointly approved last month by the FDIC and Federal Reserve Board for public comment on potential new resolution related resource requirements for large banking organizations, stating that staff will not respond substantively to any comments on the ANPR and generally will be in listening mode and will not indicate the direction the agencies are likely to take with respect to a future notice of proposed rulemaking or final rule.

### **Session 1: Integration of Supervision and Resolution**

Mr. Conneely recognized James McGraw, Senior Deputy Director, CISR; Andrew Felton, Deputy Director, Systemic Risk Branch, CISR; Alfred Seivold, Deputy Director, Institution Risk Branch, CISR; and David Wall, Assistant General Counsel, Complex Financial Institutions Section, Resolution and Receivership Branch, Legal Division, to provide an update and field questions from members on the recent work in CISR to integrate FDIC's supervisory and resolution responsibilities into the one CISR division.

Mr. Conneely started with a brief introduction of the approach utilized by CISR to integrate supervision and resolution responsibilities. He also mentioned coordination with other divisions in the FDIC, other financial regulatory agencies and internationally through the work of supervisory colleges and crisis management groups.

Mr. McGraw described CISR's organizational structure, which has brought together supervision and resolution expertise into one division. He also discussed the responsibilities of the different branches in CISR and how they work together. There was also discussion of the international coordination handled by CISR.

Mr. McGraw utilized cyber risk as an example where interaction between supervision and resolution staff is crucial.

Mr. McGraw noted the importance of information and insight obtained through supervisory staff on the Title I plan review and the Title II resolution planning processes. CISR staff has also been participating in recovery plan reviews with other banking agencies.

Mr. McGraw mentioned the responsibility for resolving nonbank financial companies and some of the inherent challenges. There will be further discussion on this topic in the context of CCPs.

Member Reed asked about informal interactions with the institutions. Mr. McGraw provided some examples.

Member Ervin asked whether there might be hesitation about turning an issue over from supervision to resolution. Mr. McGraw noted that with the creation of CISR, one team is working together and there is ongoing collaboration. Mr. Conneely added comments about some of the difficult issues and some of the successes. Mr. McGraw provided a specific example of an issue discovered during a supervisory exam that was identified as a possible resolution issue.

Member Herring noted that internationally there is a strong separation between supervision and resolution and asked whether there was a way for other countries to join the two approaches. Mr. Conneely stated that the FDIC is in a unique position in that it has supervisory and resolution authority.

Ms. Koenig discussed some of the issues and process regarding the division of supervisory authorities and resolution authorities in Europe.

Member Peterson asked about changes in expectations of the role of internal audit and the audit committees of the boards. Mr. McGraw did not think that expectations had changed. Mr. Conneely added that firms are now auditing for resolution issues.

Member Kohn asked about factors that would trigger resolution before a liquidity run. Mr. McGraw noted resolution staff is involved throughout the process, so when there is stress, preparations for an event can begin. Mr. Conneely added that the chartering authorities make the decision to close an institution but the FDIC is monitoring in real time. Mr. Felton also noted

how Title I resolution planning has improved governance mechanisms and quantitative triggers.

Member Tahyar stated that for GSIBs with single point of entry strategies, there is the concept of liquidity execution need that is calculated daily. She noted that this development is a welcome change from 2008, since a GSIB would now end up in bankruptcy before it would be closed by a chartering agency.

Member O'Connor asked how the FDIC is integrating the evolution of markets into both recovery and resolution. Mr. Connelly stated it is an area in which CISR is looking to build up its capabilities. Mr. McGraw added that he and Mr. Fulton had been working on this topic together.

Member Clark asked about efficiency of the current resolution planning process and the role of guidance versus rules in the process. Mr. Connelly said that FDIC implements the guidance and the rules and it is up to policymakers and others to determine whether guidance should be rules. Mr. McGraw added that there is a lot of authority in Title I to push firms to fix issues that have direct implications on resolution readiness.

Member Clark added to his prior question on whether the dynamic regarding resolution planning has changed due to the discussions of rulemaking through guidance.

Member O'Connor noted that financial institutions should take guidance seriously, as there is an ultimate assessment of whether plans are credible or not.

The Acting Chairman added that Title I started with rulemaking, which lays out the framework for implementing Title I authorities for resolution plans. The guidance documents provide greater detail for implementing the rule.

Director Hsu posed a question for the Committee with regard to resolution issues. He noted the challenge of keeping resolution issues from the 2008 crisis in the forefront and not turning resolution planning into a paper exercise. Director Hsu asked about what can be done to keep this issue front and center, especially as new risks arise.

Member Ervin agreed with Director Hsu that it is difficult to keep alive the memories of 2008 and to having the appropriate staffing. He suggested that training exercises could help.

Member O'Connor suggested keeping the resolution planning cycle short and doing playbook exercises.

The Acting Chairman discussed mobilizing staff in a stress environment. He noted some available resources. In the current economic environment and uncertain outlook, there is thinking about additional staffing needs on both the supervisory and resolution sides.

Ms. Koenig noted the need for training for a potential resolution situation and the importance in Europe to train with all of the national authorities for a cross border institution. She suggested testing and fire drills are the ways to prepare together.

Member Cohn noted that the 2008 crisis still heavily influences thoughts and actions. However, it is certain that the next crisis will not be a repeat of 2008, but something different. It might also happen in a much more accelerated manner than 2008 as the world is highly accelerated.

Member Clayton agreed with Member Cohn and noted that March 2020 was a little bit of a crisis- but not the same as 2008. He asked when was the last time it was all hands on deck for a resolution, even as an exercise.

Mr. Conneely thought that 2020 was an all hands on deck event and there have been market and geopolitical events with all hands on deck. He explained how the FDIC is ready all of the time for a crisis because no one knows when one will happen and it could come very fast.

Member Clayton suggested that it would be interesting to get updates on what you wished that you had during the last crisis and could be useful the next time.

Member O'Connor asked about how to horizon scan more effectively and how to think about an economy that is more open. He is not sure whether the answer is to regulate more or use existing powers of the banking agencies to identify and address risks.

Member Cohen reiterated that the FDIC does not have the data for nonbank financial institutions, which leaves an information gap as the nonbank sector grows. He asked whether FSOC could designate nonbank institutions solely for the purpose of providing data.

The Acting Chairman responded that Member Cohen raised an important question and that it is a subject that we're hoping to address.

Director Chopra noted that there are other ways of getting information for nonbank financial institutions, but also that it is incredibly difficult to use Title II for one of those institutions and not really know what is going on internally.

Mr. Conneely agreed that it is a difficult situation and the authorities are very broad. The decisions will be made at the time based on the facts and circumstances, and the parties can prepare by having discussions and making sure everyone knows their roles.

Director Hsu described the challenge of preparing for the next crisis and not the last one. He said that you need to pick the training wisely because of resources and have training that is flexible because change is happening so quickly. He noted that more creative thinking about this issue is needed.

The Acting Chairman suggested moving on to the second agenda item.

## **Session 2: Resolution Planning Update**

Mr. Conneely introduced Ryan Tetrick, Deputy Director, Resolution Readiness Branch, CISR; Elizabeth (Betsy) Falloon, Senior Advisor, Resolution Readiness Branch, CISR; Susan Baker, Corporate Expert, Systemic Risk Branch, CISR, and R. Penfield (Pen) Starke, Assistant General Counsel, Resolution & Receivership Policy Section, Resolution and Receivership Branch, Legal Division, to provide an update and respond to questions from members on Title II resolution planning for Global Systemically-Important Banks (GSIBs) and the need for greater public transparency, along with the challenges and strategic options for resolving non-GSIB large banks.

Ms. Falloon started the session by introducing the topic of transparency and explaining how CISR uses Title I plans to inform Title II resolution readiness. She also noted how CISR is building out its road map for thinking about Title II resolution. She emphasized the importance of internal tabletops and exercises. She also mentioned the coordination work with U.S. financial regulatory agencies and international supervisory and resolution authorities.



Ms. Falloon continued on the topic of transparency and whether the stakeholders understand the resolution planning process. She discussed some of the information that is available publicly with regard to Title I plans. She noted that there has been discussion of Title II issues in various venues but wants to know how FDIC can better set expectations and improve confidence in the process.

Ms. Baker continued on the theme of transparency and suggested considering which stakeholders need transparency regarding Title II resolution. She also noted that there is thinking on what messages to convey and when to convey such messages.

Ms. Baker shared a slide with potential topics for transparency and asked the Committee for feedback.

Ms. Baker continued with a question about the topics that would be helpful to put in the public domain now to improve confidence and raised questions about the Title II process generally. She also asked about how to best set expectations with public stakeholders.

Member Herring voiced appreciation for the FDIC's desire for more public disclosure. However, he was pessimistic about the FDIC's ability to communicate messages to the public because of his own experiences.

Member Herring noted that the public is less interested in the details of resolution planning. The strategy should be to disclose as much as possible to the professionals. He added that the information should generally be available so it can be readily accessed. He also noted that the general public does not have the patience to absorb all of the elaborate and careful planning that has been done.

Member Cohn agreed with Member Herring and added that the public could be scared if so much information is released. He stated that the FDIC needs to think about the unintended consequences of releasing this kind of information to a general public that has confidence in the banking system.

Member Tahyar acknowledged the work done by Ms. Falloon and Ms. Baker on this issue. She stated that there is more information that can be made public without being scary, and that timing is part of the issue. Member Tahyar also noted that transparency leads to accountability.

Member Tayhar added that now there is an additional group of stakeholders that need to know more about resolution planning, e.g, fintech nonbank lenders, digital assets, etc. She suggested that making more information public is good, but maybe not everything.

Ms. Koenig described her experiences trying to achieve more transparency in Europe. She noted that parties need to be mindful about timing when making the information public.

Member O'Connor made suggestions regarding the types of communications that would be useful and appropriate.

Member Ervin noted the need for fast communications and the appropriate communications for the various stakeholders.

Member La Salla commented on the need for accurate information.

Member Clayton also noted the effect of economic conditions on how statements will be treated by the public.

Member Kohn wondered whether there are market tests that might show whether transparency in resolution planning is having an effect on the market.

Director Hsu made further comments about setting expectations and making stabilizing statements.

Member Peterson thought the most stabilizing comments have come from the CCAR tests. He noted that information should be geared towards professional investors, but also available to anyone.

Member Ervin made further comments regarding the capital markets.

Member Herring described his experience on the Committee with regard to market reactions.

Mr. Conneely turned the floor over to Mr. Tetrick to discuss the resolution of non-GSIB large banks.

Mr. Tetrick started by acknowledging that this is the first discussion of a large bank resolution in the SRAC, and further discussed the meaningful steps the FDIC has taken to improve resolvability of large banks, including regional banks and domestic systemically important banks. Mr. Tetrick further discussed how the FDIC handled the failure of the largest

insured depository institutions (IDIs) during the global financial crisis.

Mr. Tetrick shared a slide discussing the Federal Deposit Insurance Act (FDIA) authority under which IDIs would be resolved, including a discussion of the least cost test and the Deposit Insurance Fund.

Mr. Tetrick shared a slide discussing resolution under the FDIA authority as it pertains to IDIs with over 100 billion dollars in assets, versus IDIs with over 250 billion dollars in assets, and the impact of institution size, complexity, and operational continuity on resolution, as well as foreign affiliates and foreign banking organizations of U.S. IDI subsidiaries.

Mr. Tetrick shared a slide showcasing the unique challenges from a resolution perspective for large banks, as distinguished from resolution of both global systemically important banks (G-SIBs) under Title II of the Dodd-Frank Act, and the resolution of ordinary community banks. The challenges that Mr. Tetrick discussed ranged from necessary capital and operational resources, loss absorbency, implementation of bridge bank strategies, receivership management and the receivership entity the FDIC would be responsible for, as well as projections about valuations from failure through the course of the bridge period.

Mr. Tetrick discussed the FDIC's two resolution specific record keeping requirements related to large bank resolution, as well as the FDIC's IDI specific resolution planning requirement.

Member Mayopoulos commented on the scale of failure and the likely cause being a macro event likely to affect multiple institutions at once, and asked about the ability to collectively coordinate all of that with possible knock-on effects.

Mr. Tetrick responded that the focus is on strategies that reduce the resource need of the FDIC, and that there is decision making with other authorities to manage failures at multiple institutions. Mr. Tetrick further discussed the related challenges, and knock-on effects to uninsured depositors.

Member Ervin commented that additional challenges would include the need for acquirers, especially given that interested foreign banks may find it more expensive to operate cross border, and other legal issues such as existing litigations that may accompany an acquisition.

Mr. Tetrick responded that the FDIC is looking at opportunities to expand the range of scenarios for an acquirer, and will also look into legal risk.

Member Clayton commented that WaMu's failure happened quickly, and there was an option to retain certain liabilities in the receivership and pay them pursuant to the priority scheme.

Member O'Connor commented on how Title I and Title II resolution plans for G-SIBs compared to the discussion on large bank resolution, and the correlation between bank size and risk. Member O'Connor further commented on being careful of bailouts and moral hazards.

Member Tahyar commented on the ANPR, and being carefully balanced in the imposition of long term debt in a rising interest rate environment. Member Tahyar further discussed consideration of uninsured deposits being brokered deposits, or a small business payroll, and suggested careful thinking around the ANPR.

Ms. Koenig commented on what makes a successful resolution, and finding a qualified buyer and timing. Ms. Koenig further discussed increasing optionality without jeopardizing the firm.

Member Ervin commented on the differences in Europe and UK with respect to MREL, and internalizing an externality and cost of dealing with a contingency.

Member Tahyar commented on the tool of contingent capital and the effect of it being a tax blocker.

Member Herring commented on the prior GSIB scores of all of the major U.S. banks, and how they indicated that these institutions were different.

Mr. Tetrick commented on systemic risk and how it depends on the scenario. Mr. Tetrick also shared a slide discussing outlining the three strategic options for a large bank resolution, and that the focus would be on the second option, a bridge bank, as opposed to a sale to a third party acquirer or liquidation. Mr. Tetrick further discussed deposits passing in a bridge, the least cost test, and franchise value. Mr. Tetrick also discussed bridge strategy, including ways to exit from the bridge and timing.

Mr. Tetrick shared a slide discussing some of the things the FDIC is doing to enhance large bank resolvability, including the IDI resolution planning process, joint feedback with the Federal Reserve to provide guidance to some of the largest banks that file Title I resolution plans, and the ANPR on long-term debt.

Member Ervin asked whether there was a dividing line in terms of the systemic risk scores, and expressed concern of the continuity to the U.S. banking system. Member Ervin further elaborated that U.S. G-SIBs have remained the same since designated, and that other banks have stayed within their buckets, and that there may be instances where the system could work smoother and provide optionality amongst banks that are similar in size but that fall in separate buckets.

Member Peterson commented that there are other considerations in addition to size.

Mr. Tetrick commented that some regional banks are larger than some G-SIBs based on scores and sizes, and that consideration is also given to complexity of the activities and cross border activity.

Member Peterson commented that size is only one-fifth of the G6.

At the conclusion of this discussion, the meeting stood in recess from 11:14 a.m. to 11:26 a.m.

### **Session 3: Central Counterparty Resolution Challenges**

Mr. Conneely recognized Jennifer Traille, Associate Director, Systemic Risk Branch, CISR, and Sir Jon Cunliffe, Deputy Governor for Financial Stability, Bank of England and Chair of the BIS Committee on Payments and Market Infrastructure (CPMI), to provide an overview of the challenges associated with the resolution of Central Counterparties (CCPs).

Ms. Traille started the session by revisiting the topic of CCP resolution under Title II that was discussed in the last SRAC meeting in 2020. Ms. Traille continued by stating the focus would be on key challenges faced domestically in thinking about resolving one of these institutions, and highlighted the ongoing work that the FDIC is involved in internationally to address some common challenges across authorities and jurisdictions.

Ms. Traille discussed the first challenge of CCP resolution being a lack of resources that are available to support a CCP resolution. Ms. Traille further discussed that the FDIC has authority to use the tools and resources within the CCP's rule book in Title II, however their application or availability would be weighed against financial stability consequences. Ms. Traille further elaborated that unlike SPOE for G-SIBs, CCPs do not have financial resources available to absorb losses and recapitalize a firm to ensure operational continuity of critical functions for the market during a resolution.

Ms. Traille discussed the second challenge of CCP resolution being the lack of a requirement for CCPs to file resolution plans with the FDIC, and how this is contrasted to G-SIBs that are required to file resolution plans under Title I. Ms. Traille elaborated that the resolution plans have not only greatly informed the FDIC's resolution planning and resolution readiness under Title II along with firm engagement and capabilities testing, but have also been beneficial to the firms in developing capabilities that have proven useful both in business as usual and in stress.

Ms. Traille discussed the third challenge of CCP resolution being that the FDIC does not benefit from a direct resolution engagement with CCPs given that the FDIC relies on the supervisory authorities of other U.S. regulatory counterparts. Ms. Traille further elaborated that this informs the FDIC's understanding of CCP resolvability, and prohibits the FDIC from directly removing the barriers to CCP resolution, or proactively enhancing the resolvability of the CCPs. Ms. Traille continued that the FDIC has worked with U.S. regulatory counterparts and within the FDIC's existing authorities to make progress in Title II resolution planning, better understanding the supervisory monitoring and actions during business as usual, and to develop ex-ante frameworks and legal documents to support resolution planning.

Ms. Traille shared a slide discussing the FDIC's involvement on the international front to further progress in CCP resolution. Ms. Traille discussed the FDIC's participation in international standard setting bodies, as well as the FDIC's direct engagement with foreign supervisory and resolution authorities through bilateral and multilateral workstreams. Ms. Traille discussed the role of the Financial Stability Board (FSB), and the FDIC's involvement with the FSB including Acting Chairman Gruenberg's chairing the FSB's resolution steering group and Art Murton co-chairing the working group on FMI cross border crisis

management. Ms. Traille further discussed the FSB's series of joint workshops over the last two years with the Committee on Payments and Market Infrastructure (CPMI), the International Organization of Securities Commissions (IOSCO), and the Basel Committee on Banking Supervision (BCBS). Ms. Traille also discussed the FSB guidance of November 2020 that laid out a framework for authorities with respect to supporting an orderly resolution, which led to further work by the chairs of the FSB, CPMI, and IOSCO on financial resources for both recovery and resolution. Ms. Traille further discussed that there was a report published in March 2022 that was part of an effort to determine future policy work on the subject.

Ms. Traille highlighted other venues in which the FDIC works with foreign counterparts on CCP resolution, including U.S.-UK principal level engagement among the Bank of England, Board of Governors of the Federal Reserve System (FRB), the U.S. Securities and Exchange Commission (SEC), the Commodity Futures Trading Commission (CFTC), and the FDIC. Ms. Traille also discussed the FDIC's role in hosting crisis management groups jointly with the CFTC and SEC for the three U.S. CCPs, in which both U.S. and foreign regulatory authorities participate, and how these meetings are valuable to understand shared challenges, share approaches and progress, and to try to identify improved resolution options.

The Acting Chairman thanked Ms. Traille for laying out the background and context before turning to the guest speaker, Sir Jon Cunliffe. Mr. Gruenberg provided an introduction of Mr. Cunliffe, the Deputy Governor of the Bank of England for financial stability, and discussed the collaborative work on resolution issues done with Mr. Cunliffe in the past.

Mr. Cunliffe started the session with a description of what he does as Deputy Governor for Financial Stability, including his micro-prudential and macro-prudential responsibilities for CCPs, settlement systems, and payment systems for supervision and regulation. Mr. Cunliffe stated that he will speak from the perspective of the FSOC from a financial stability perspective, and the CFTC and the SEC and CCP regulator perspective. Mr. Cunliffe stated that he would set out why effective regimes are needed to deal with CCP failures, why CCPs are different than banks, and the risks they take and how they manage them, and what the UK regime will do.

Mr. Cunliffe discussed CCP's role, and what makes them systemic. Mr. Cunliffe further discussed that the mandate of CCPs for some

key financial derivatives following the great financial crisis have made them more systemic globally. Mr. Cunliffe discussed the role of CCPs in commodity markets and in hedging and forward contracts.

Mr. Cunliffe continued that given the CCPs are not banks, and role they play, the design of any resolution framework needs to reflect some of the essential differences. The first difference Mr. Cunliffe discussed is that the risks that CCPs run are very different than the risks in banks. Mr. Cunliffe elaborated that the two risks CCPs face are essentially counterparty credit risk, and operational risk of some sort of operational failure.

Mr. Cunliffe discussed counterparty credit risks, describing that CCPs would need to be able to absorb losses to restore matchbook, by both using the prepositioned resources of the defaulting members, and effectively passing losses with limits back to their clearing members through both a default fund and making cash calls. Mr. Cunliffe explained that unlike banks, CCPs cannot go bankrupt with respect to default losses.

Mr. Cunliffe discussed non-default operational losses, such as fraud, cyber, or investment losses. Mr. Cunliffe elaborated that CCPs generally have no power to pass those losses on to members, and that they have to be absorbed by CCP capital, which could ultimately lead to CCP insolvency.

Mr. Cunliffe discussed how resolution should address the two risks discussed, and that even with respect to default losses, the CCP rule book allows for an effective wind down of the CCP without bankruptcy. Mr. Cunliffe discussed the impact on financial markets if clearing services are lost, and the recovery action choices of CCP management.

Mr. Cunliffe discussed the importance of the resolution authority taking control prior to the exhaustion of CCP recovery actions, so that the resolution authority is able to use the CCP recovery tools flexibly. Mr. Cunliffe further discussed the need for additional resolution tools for the resolution authority, as well as a resolution plan.

Mr. Cunliffe discussed the current UK regime with respect to CCP resolution, and what the legislation that is now going through Parliament will grant to the UK regime, such as extra powers that do not currently exist in some of the CCP rule books.



Mr. Cunliffe raised the question, for default losses, is there a need for extra pre-funded resources in recovery or resolution to supplement what already exists. Mr. Cunliffe raised two reasons why an increase in the pre-funded resources in the CCP may be beneficial. Mr. Cunliffe discussed the first reason being the question of incentives, as CCP equity is not going to be written down, and therefore it is important for CCPs to have skin in the game. Mr. Cunliffe further elaborated that the key objective is to ensure that the incentives are sufficient and rightly placed to avoid resolution by incentivizing CCP management.

Mr. Cunliffe discussed the second reason of why an increase in pre-funded resources in the CCP may be beneficial as being to ensure that there are enough resources in resolution so that the CCP does not have to rely on cash calls, haircutting the variation margin, or in the later stages tear up contracts once the resolution authority comes in. Mr. Cunliffe further elaborated on an option to raise extra resources for the CCP by issuing bailout bonds, and why that may be preferably to cash calls and the cutting of margin and other tools.

Mr. Cunliffe continued that this complex debate would be informed by the first stage of the international work which looked at pre-funded and non-prefunded resources in a number of systemic CCP's ability to absorb losses in recovery and resolution. Mr. Cunliffe elaborated that the work had suggested that the systemic CCPs could absorb failure of up to four of their largest clearing members, above the international standard of two large clearing members. Mr. Cunliffe further explained that the cash calls would be within the capacity of the remaining clearing members which tend to be the larger financial institutions, and if they resist these cash calls they would effectively be in default, which is unlikely.

Mr. Cunliffe continued that if three or four of the largest clearing members fail, that this would impact not just one CCP, but across the board and across the financial system. Mr. Cunliffe further discussed that if two to four G-SIBs also failed, the resolution would enable those members to continue to meet their obligations to a CCP without default. Mr. Cunliffe stated that in the end, it is a question of how far into the tale of risk distribution should be explored with protection, and do the costs outweigh the benefits.

Mr. Cunliffe discussed an example of if CCP issued bonds were to equal the default bonds, the CCP would have a full reload in resolution, however the annual coupon of the issued bonds could

be equal or greater than the CCP's capital. Mr. Cunliffe discussed that these costs would likely be passed back to the CCP users. Mr. Cunliffe stated that the benefits would need to be measured against the costs. Mr. Cunliffe further discussed that in some circumstances, a reservoir of pre-funded resources that can be accessed only in resolution might be necessary to enable CCP clearing services to continue to operate.

Mr. Cunliffe discussed non-default losses, and that the capital to absorb these losses is limited, and so the resolution authority would need access to other resources separate from the waterfall. Mr. Cunliffe further discussed that in the UK, new powers are being considered by Parliament that would allow the resolution authority to make a cash call in order to absorb non-default losses or recapitalize the CCP. Mr. Cunliffe further discussed the importance of a resolution authority having access to some resources to keep the clearing service in operation.

Mr. Cunliffe concluded that the CPMI-IOSCO standards are for the operation of CCPs, and do not include resolution. Mr. Cunliffe elaborated the need to think about recovery and whether CCPs should have better options to deal with non-default losses.

The Acting Chairman thanked Mr. Cunliffe for the lucid presentation on a pretty complicated subject, and asked if there were questions from members of the committee.

Mr. Herring thanked Mr. Cunliffe for the terrific overview, and stated that in a bank resolution, there is hope to have a resolution weekend. Mr. Herring asked how the shorter time for action will be dealt with given that with a CCP there is almost no time to intervene and try to take control of the situation to keep it from deteriorating quickly.

Mr. Cunliffe responded that this was a real challenge, and in circumstances in which two clearing members have defaulted there would be a situation of general stress given very fast moving markets. Mr. Cunliffe stated that there is a case for the resolution authority to be closely involved with the business of the CCP, as well as to have close cooperation with the CCP supervisors. Mr. Cunliffe also stated that the resolution plan has to have stabilization.

Mr. Cunliffe discussed past defaults, and how CCPs were able to go through the default waterfall quickly, such as in the case with Lehman Brothers. Mr. Cunliffe continued that the UK will do some dry runs and resolution testing.

Member Ervin thanked Mr. Cunliffe on a terrific presentation on a tough subject. Member Ervin asked whether minimum initial margins could be a solution if there are different types of waterfalls, and if equity is not being wiped out, how would incentives align of the CCP towards systemically positive events, and how would alignment be improved going forward.

Mr. Cunliffe discussed the need to look at the responsiveness of CCP margins to shocks, and whether there should be a calling of margin more prudently in good times or normal times so that the jump to stress margin is not so great in their terms. Mr. Cunliffe further discussed the interest in looking at the responsiveness of CCP margin models, and the hope to receive views on how to measure pro-cyclicality of margin and stress, which is what will cause default.

Mr. Cunliffe discussed the problem with equity if the CCP is subject to no creditor worse off protection, and if the CCP's rule book states that the CCP can make unlimited calls on its members and then wind itself and still preserve equity. Mr. Cunliffe continued that this cannot be squared with writing down the equity and resolution with a no creditor worse off guarantee, and stated that consideration would be given to whether the no credit worse off guarantee should offer that level of protection to shareholders in terms of incentives.

Member O'Connor inquired how the non-default losses and the resolution authority having the ability to make a cash call were being considered given that the risks occurring are solely brought on board by the CCP management. Member O'Connor further added that the discussion is about de-neutralizing CCPs, not neutralizing CCPs, and questioned the backstop of doing a cash call of clearing members that have no engagement in the CCP's risk management.

Mr. Cunliffe responded that whether pre-funded resources or a cash call, there is a clearing obligation and mandate on the services, and that the costs are going to be passed back to users. Mr. Cunliffe further explained that if non-default losses wipe out CCP equity, there would be an incentive effect, and members would need the clearing services to continue. Mr. Cunliffe stated that public sector support would likely want to be avoided.

Mr. Cunliffe continued in discussing that members would own the clearing services in the event there was a resolution where a

CCP's capital is wiped out by members, the losses are absorbed by the cash call, and the CCP is recapitalized by the cash call. Mr. Cunliffe discussed that the more members are exposed to these risks, the more they will demand, and there needs to be more involvement in risk management and an understanding of CCPs' expectations.

Mr. Cunliffe discussed how CCPs have informed regulators that there is pressure from their members to charge less margin, and to reduce the costs of failing all the time. Mr. Cunliffe further discussed that clearing members at senior levels are worried about the CCPs' risks and not having influence over CCPs.

Member O'Connor asked if, with respect to up front resources, and inclusive of bail-in-able debt, this was really the preferred recapitalization mechanism because it moves from a demutualized to a mutualized model. Member O'Connor further inquired why is the collective having a hard time if everyone says they want more pre-funded, more TLAC, and better collateral.

Mr. Cunliffe responded that there are reports that CCP clearing members are under pressure to complete a margin because the clearing members will go to the cheaper action, and pre-funded resources costs money, and such costs are going to come back to members. Mr. Cunliffe discussed the need for more transparency around margin models and their pro-cyclicality, how they will react in stress so clearing members may plan for it, and metrics so that clearing members have a view on whether they want to use CCPs with more or less pro-cyclical models. Mr. Cunliffe also discussed the need for regulators to think about whether to adopt a prefunded approach, or whether there should be a use of margin models that attune between pre-stress and stress.

Member O'Connor responded that he agreed with Mr. Cunliffe, and would suggest that clearing members raise certain issues that are related to risk, whether it's margin or collateral, or things of that nature. Member O'Connor further stated that there is a need for transparency so that regulators can be helpful in understanding the risks that are coming on board.

Mr. Cunliffe responded that he agreed with Mr. O'Connor, and discussed the need for regulators to have the power to be able to make those decisions, and that different jurisdictions have regulators who have different powers for the approval or not of

new clearing products. Mr. Cunliffe concluded that he thinks there is a need for more options in the future.

The Acting Chairman thanked Mr. Cunliffe for his superb overview of an important issue, and this will be an ongoing issue and matter of attention for the FDIC and will be brought back to committee as well.

Mr. Cunliffe thanked the Acting Chairman for the information and for taking on the international work, as these are basically global infrastructures that the regulators need to manage.

Member Reed discussed the contrast between the Bank of England work on CCP's and the procedural progress being made in the U.S., and asked whether the U.S. regulators have the capability to deal in a timely manner with a CCP serious trouble.

The Acting Chairman stated that he would be glad to respond, but will give Ms. Traille the first response.

Ms. Traille responded that a number of the challenges had been highlighted during the session, including the likelihood that runways would be short. Ms. Traille continued that the FDIC would need to look at the existing planning, and its existing authorities and tools. Ms. Traille also mentioned procedure, and how the FDIC works with supervisors and other authorities to build its understanding and information. Ms. Traille mentioned the work on planning for individual firms, and the acknowledgement that there are challenges and more work to be done, such as planning to operationalize the strategy to preserve the CCP's critical operations for the market.

The Acting Chairman discussed the gap on the resolution side relating to non-bank financial companies, and that Dodd-Frank put in place a coherent framework of authorities for agencies to deal with the resolution of a global systemic banking organization through the Title II orderly liquidation fund backstop, and Title I resolution plans. The Acting Chairman further discussed the progress made domestically and internationally on TLAC additional loss absorbing resources, as well as in terms of cross border cooperation in light of both Ms. Koenig's and Mr. Cunliffe's presence at the meeting.

The Acting Chairman continued that a fairly credible framework has been built that has not been tested or executed yet in practice, and that until it is, caution must be exercised with respect to making representations. The Acting Chairman further

discussed the authorities, capabilities, and resources across international relationships that did not exist prior to 2008, that put the FDIC in a different place.

The Acting Chairman stated that the FDIC would bring the default Title II authorities to bear for a systemic firm failure, whether it's for a bank or nonbank, but that supervision responsibilities are in the market regulators. The Acting Chairman discussed the future work to do in both the U.S. and the international side, and that putting in place the framework and infrastructure on the nonbank side should probably be where attention and priority is place in a post-crisis world.

Member Clayton commented that he agreed with the Acting Chairman, and that the members of the CCPs are the entities that are being looked at, and therefore CCP resolution cannot be considered in isolation from resolution of financial institutions because they are going to happen at the same time.

Member O'Connor commented on the good news that in most financial institutions resolution recovery plans, their largest counterparty exposures are included. Member O'Connor discussed ways in which the model may become less stable from the centralized approach, and restrictions of clearing members versus end users. Member O'Connor further discussed variation margin haircutting, and the equivalent in the bank recovery and resolution plan space versus the CCP space. Member O'Connor concluded that this really important work should continue.

The Acting Chairman asked if there was anything else for today's meeting.

### **Closing Remarks**

Following the presentations and all of the related discussion, Acting Chairman Gruenberg thanked the members for participating in the meeting and for their very helpful feedback. He expressed that he is looking forward to meeting with the Committee again next year.

There being no further business, the meeting was adjourned at 12:33 p.m.

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Debra A. Decker  
Executive Secretary  
and Committee Management Officer  
Federal Deposit Insurance Corporation  
FDIC Systemic Resolution Advisory  
Committee

Minutes  
of  
The Meeting of the Systemic Resolution Advisory Committee  
of the  
Federal Deposit Insurance Corporation  
Held in the Board Room  
Federal Deposit Insurance Corporation Building  
Washington, D.C.  
Open to Public Observation via Webcast  
November 9, 2022 – 9:00 A.M.

I hereby certify that, to the best of my knowledge, the attached minutes are accurate and complete.

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Martin J. Gruenberg  
Chairman  
Board of Directors  
Federal Deposit Insurance Corporation