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Resolution Planning: The National, International and Strategic Context

by Gregory Lyons, David Luigs, Pratin Vallabhaneni and Samuel Proctor

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On November 1, 2011, the Federal Deposit Insurance Corporation (the "FDIC"), jointly with the Board of Governors of the Federal Reserve System (the "Board") (together, the "Agencies"), published a final rule (the "Living Wills Rule"), implementing the resolution plan requirements of Section 165(d)(1) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act").[1] Section 165(d)(1) of the Dodd-Frank Act requires each nonbank financial company supervised by the Board and each organization subject to the U.S. bank holding company ("BHC") rules with assets of $50 billion or more (each, a "Covered Company") to report periodically to the Board, the FDIC, and the Financial Stability Oversight Council (the "FSOC") the Covered Company's plan for a rapid and orderly resolution in the event of material distress or failure.

Also on September 9, 2011, as a complement to the Living Wills Rule, the FDIC adopted an interim final rule (the "IDI Rule"), which requires any FDIC-insured depository institution with $50 billion or more in total assets (a "CIDI") to submit periodically to the FDIC a contingency plan for the resolution of such institution in the event of its failure.[2] The FDIC was not required to promulgate the IDI Rule pursuant to the Dodd-Frank Act, but rather chose to do so using its authority under the Federal Deposit Insurance Act (the "FDI Act"), which gives the FDIC broad authority to carry out its statutory responsibilities and to obtain information necessary to do so.[3] The Living Wills Rule and the IDI Rule (together, the "Resolution Plan Rules") become effective on November 30, 2011 and January 1, 2012, respectively.

The Resolution Plan Rules not only implement the resolution plan mandate of Section 165(d)(1) of the Dodd-Frank Act, but also respond to calls for "internationally-consistent firm-specific contingency and resolution plans."[4] Although the Living Wills Rule is final, the IDI Rule is subject to further comment, and the Agencies intend to issue subsequent guidance and resolution plan templates that will likely take into account ongoing international initiatives in the area of cross-border resolution planning. Our discussions with the Agencies also reveal their willingness to work with the industry to formulate acceptable templates from which resolution plans may be modeled.

In this article, recognizing that international initiatives have already influenced the Resolution Plan Rules, we first proceed to describe the international context in which the Resolution Plan Rules were promulgated. We then summarize the specific provisions of the Resolution Plan Rules. We lastly offer an analysis of how covered companies may seek to leverage the Resolution Plan Rules for their strategic benefit. Throughout this article, our analysis is appropriately informed by our ongoing representation of the Financial Services Roundtable (the "FSR"), on whose behalf (in addition to others) we have met with staff from the Agencies on several occasions both before and after publication of the Resolution Plan Rules.

Resolution Planning on the International Level

In the wake of the recent financial crisis, governments across the globe began to think more seriously about implementing effective resolution regimes that could help end the "too big to fail" phenomenon. The U.S., one of the first movers in this regard, is implementing its resolution

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Letter from the Editor

A little over a year after the passage of Dodd-Frank, regulators are starting to publish some of the most significant rules for the largest U.S. banking institutions required by Title I of the statute. In this issue, we focus on two of the most significant rules to date - the rules regarding Living Wills, which is final, and the proposed designation process for Non-bank Systematically Important Financial Institutions, or "SIFIs." The Living Wills article also discusses how in many circumstances U.S. regulators are seeking to work with their international counterparts to create relatively uniform regimes to minimize risks to the global economy posed by the largest financial institutions. We expect to see more of these major initiatives in the upcoming months, including the Market Risk proposals, the Dodd-Frank "prudential rules" for the largest institutions, and efforts regarding shadow banking and central counterparties. We intend to continue informing you of both the implications of the rules themselves and their interplay with global frameworks.

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Co-Editor-in-Chief

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FSOC Releases Proposed Rule and Guidance on its Process to Designate Non-bank Firms as Systemically Significant

*by Satish M. Kini, David A. Luigs and Elizabeth B. Alspector**

On October 18, the Financial Stability Oversight Council ("FSOC") published in the Federal Register a proposed rule and interpretive guidance regarding the process and criteria by which it may designate a non-bank financial firm as systemically important and, thus, subject to increased regulatory oversight. The proposed rule is intended to provide greater clarity and specificity regarding the criteria the FSOC will apply in making those determinations, which had largely been lacking in a prior much-criticized FSOC proposal. Comments on the proposed rule and interpretive guidance are due December 19, 2011.

Background

Section 113 of the Dodd-Frank Act authorizes the FSOC to designate non-bank financial firms that it believes could "pose a threat to the financial stability of the United States." The Dodd-Frank Act subjects such designated firms to supervision by the Federal Reserve under certain enhanced prudential requirements. The Act lists ten expansively worded factors that the FSOC may use to make a systemically important financial institution ("SIFI") designation – ranging from the amount and nature of a company's financial assets to the company's reliance on short-term credit to "any other risk-related factor FSOC finds appropriate."

In January 2011, the FSOC issued its first proposed rule on this topic, which principally provided insights on how it proposed to proceed as a matter of process and procedures. The January 2011 proposal offered virtually no details as to how the FSOC would interpret and apply the statutory criteria to firms, *e.g.* which criteria might be given greater or lesser weight. This opacity, which appeared deliberately designed to maximize the FSOC's flexibility in the SIFI designation process, was harshly criticized by industry and on Capitol Hill. In response, in particular to congressional pressure, the FSOC promised additional details regarding how it intended to apply the statutory criteria to assess and designate non-bank financial firms. The FSOC's new proposal seeks to fulfill that promise.

Proposed Three-Stage Process

In its new guidance, the FSOC proposes to use a three-stage process for SIFI designation. Stage 1 would be a screening phase involving publicly available data; Stage 2 would involve a deeper review of firms that clear the Stage 1 screen of additional information based on additional metrics, including data from relevant government agencies; and Stage 3 would involve information obtained directly from, and participation by, the potential designee itself.

The three-stage process is set forth principally in guidance, not in the FSOC's proposed regulation. Thus, as a matter of administrative law, the FSOC may be able to change the guidance in the future without resort to formal notice and comment procedures. Whether or not that is true as a matter of administrative law, the FSOC suggests that it will revise the guidance only through notice and comment procedures, which seems likely as well given the political dynamics and intense interest the guidance has and will continue to garner.

Stage 1. During Stage 1, the FSOC proposes to apply six uniform quantitative thresholds to financial firms. In the Stage 1 process, the FSOC proposes to apply thresholds that relate to size, interconnectedness, leverage and liquidity risk/maturity mismatch. The first threshold relates to asset size:

- *Size.* The FSOC has proposed a size threshold of $50 billion in assets. For U.S. firms, the threshold would apply to global total consolidated assets, and for non-U.S. firms, the threshold would apply to U.S. total consolidated assets. This $50 billion test is taken from the Dodd-Frank Act, which generally subjects banking firms with $50 billion or more in assets to enhanced supervision and regulation. The release does not explicitly address whether assets

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under management are included in calculating the size threshold.

A firm meeting the size threshold plus at least one of the following would be subject to review under Stage 2:

- *Credit Default Swaps Outstanding.* The FSOC proposes to apply a threshold of $30 billion in gross notional credit default swaps ("CDS") outstanding for which the nonbank company is the reference entity. To some, this threshold is potentially problematic because it is based on third-party decisions to write CDS on a financial firm, over which the firm has no control.

- *Derivative Liabilities.* The FSOC proposes a threshold of $3.5 billion of derivative liabilities. Derivative liabilities would be calculated as the fair value of any derivatives contracts in a negative position, after taking into account the effects of master netting agreements and cash collateral held with the same counterparty on a net basis, if elected. The FSOC acknowledged that this threshold would only capture current derivative exposures, and the FSOC said it would establish a new threshold based on potential future exposures after the Commodity Futures Trading Commission ("CFTC") and Securities and Exchange Commission ("SEC") finalize their rules on swaps and security-based swaps reporting.

- *Loans and Bonds Outstanding.* The FSOC intends to apply a test of $20 billion in outstanding loans or bonds issued. In proposing this threshold, the FSOC argued that a large amount of loans and bonds outstanding serves as a proxy for interconnectedness.

It seems unlikely that the FSOC will issue a final rule and guidelines until spring 2012. If so, the first designations probably will not take place until summer 2012, a pace that is substantially slower than many had expected when the Dodd-Frank Act was first enacted.

- *Leverage Ratio.* The FSOC proposes to apply a leverage ratio of total consolidated assets to total equity of 15:1. Insurance separate accounts would not count as consolidated assets for purposes of this test.

- *Short-term Debt Ratio.* The FSOC intends to apply a threshold ratio of short-term debt to total consolidated assets (excluding separate accounts) of 10%. For this purpose, short-term debt would be debt with a maturity of less than one year.

Because these metrics would generally be based on publicly available data, they may permit interested observers to determine which firms are likely to pass through Stage 1 and on to ensuing stages. Some analysts have already produced reports identifying such firms.

Although the Stage 1 approach is designed to introduce transparency and a level of certainty to the process, the FSOC has not completely abandoned discretion (and the resultant opacity). Indeed, some aspects of the Stage 1 methodology remain ambiguous. First, the FSOC stated that because the proposed metrics might not capture all firms, it may "in limited cases" evaluate a potential SIFI based on "other firm-specific qualitative or quantitative factors." No guidance is given, however, on when these firm-specific criteria could be triggered.

Additionally, the FSOC suggests that the proposed quantitative thresholds may not be appropriate for a subset of nonbanking financial companies. For example, using additional data gathered about hedge funds and private equity firms from newly adopted Form PF, the FSOC will consider whether to establish additional metrics or thresholds for these firms. In addition, and more broadly, the FSOC says it may propose additional criteria for asset managers in general. The guidance, in a footnote, notes that multiple investment funds managed by one nonbank financial company may be considered a single entity if the funds' investments are identical or highly similar.

Stage 2. The FSOC proposes

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to conduct a comprehensive analysis of firms that clear Stage 1, including through the use of industry- and firm-specific factors. Stage 2 analysis would include publicly available information plus information obtained from regulators and from the company voluntarily. The suggestion that a firm may voluntarily supply information in Stage 2 would appear to mean that a firm would be informed of its consideration under this stage, although the FSOC's proposal is not explicit on this point.

The analysis in Stage 2 would be based on a six-category framework, described originally in the FSOC's first proposed rule in January. As in that release, the first three of these factors pertain to the potential impact of the company's financial distress on the broader economy; the second three seek to address the potential vulnerability of the firm to distress. The new proposed rule provides greater color on each of the six factors than the January release, especially with respect to how the FSOC would measure those factors, as follows:

1. *Interconnectedness.* According to the FSOC, interconnectedness would capture the direct or indirect linkages between financial companies that could transmit the negative effects of a firm under material financial distress to others. Interconnectedness would be measured by, for example, reviewing counterparty exposures to a firm, including derivatives and other exposures and assessing the number, size and financial strength of a firm's counterparties.

2. *Substitutability.* Substitutability would capture the extent to which other firms could provide equivalent financial services quickly and at a similar price and quantity if a firm left a particular market. This factor would look to such factors as the market share of the firm and its competitors across different time periods and for different products or services.

3. *Size.* Size would capture the amount of financial services or intermediation that a firm provides. The FSOC proposes to measure size by reference not only to the traditional metrics of assets, liabilities and capital, but also other metrics such as off-balance-sheet assets and liabilities and numbers of customers and counterparties.

4. Leverage. Leverage would assess a firm's exposure or risk in relation to its equity capital. It would be measured by the traditional ratio of debt to capital and also by reference to the ratio of economic risk relative to capital. To make this second measurement, the FSOC proposes to consider derivatives and off-balance sheet exposures and other products with embedded leverage.

5. *Liquidity Risk and Maturity Mismatch.* Liquidity risk would measure the risk that a firm may not have sufficient funding to satisfy its short-term needs. Maturity mismatch would measure the difference between the maturities of an firm's assets and liabilities.

6. *Existing Regulatory Scrutiny.* Finally, the FSOC proposes to assess the existing regulatory scrutiny to which a firm is subject.

In addition, the FSOC has proposed that, in Stage 2, it would review whether the resolution of a non-bank financial firm could pose a threat to U.S. financial stability. The FSOC noted in the guidance that it may apply the Stage 2 criteria in the "context of stressed market conditions."

As the FSOC has made clear, it intends the analysis in Stage 2 not to be formulaic but specific to each company. The FSOC proposes that, based on the analysis in Stage 2, it will choose which firms to review in Stage 3.

Stage 3. The FSOC would contact companies that are identified for review at Stage 3. Such firms would receive a "Notice of Consideration," which will likely ask the firm to provide additional non-public information to FSOC. Firms that find themselves in Stage 3 analyses likely will need to provide significant information to the FSOC to avoid a SIFI designation. Firms also may be able to negotiate with the FSOC and avoid a potential designation by, for example, ceasing certain activities or engaging in certain risk-mitigation practices.

The FSOC proposes that Stage 3 would build on the analysis completed in Stage 2 and consider

FSOC Releases Proposed Rule and Guidance

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qualitative information collected from either other agencies or the potential SIFI, if requested in the Notice of Consideration. Factors the FSOC proposes to consider in Stage 3 include the resolvability of the firm, the opacity of its operations, its complexity and the extent to which it is already subject to regulatory scrutiny.

The FSOC must confer and vote (by two-thirds majority, including the FSOC's Chairperson, the Secretary of the Treasury) on the proposed designation of a firm. Prior to making such a proposed designation, the FSOC says it may confer with the firm's primary regulator or home-country supervisor and consider the firm's views. The FSOC makes clear, however, that it would not be bound by those regulator views.

Designations

If the FSOC determines by the requisite two-thirds vote that a firm should be designated as a SIFI, the final step is to issue a Notice of Designation to the firm, which allows the firm an evidentiary hearing and, subsequently, resort to judicial review. At the evidentiary hearing, the FSOC will determine again by a vote of two-thirds of its members, including an affirmative vote of the Chairperson, whether to issue a final designation. The FSOC is required to reevaluate each designation annually and to rescind a designation by a two-thirds vote if a company no longer meets the proposed rule's requirements.

Confidentiality

Following the release of the FSOC's first proposed rule, many companies were concerned that confidential company information provided by the company to the FSOC would be publicly available under the Freedom of Information Act ("FOIA"). In response to these concerns, in the second proposed rule, the FSOC requires that any "data, information, and reports" submitted to the FSOC by companies under review be maintained as confidential. Additionally, any "non-publicly available data or information" submitted would not constitute a waiver of privilege under federal or state law. Nonetheless, the proposed rule provides that any information submitted by a company under review remains subject to the provisions of FOIA.

Emergency Exception

The FSOC also included an emergency exception to the three-stage process in the second proposed rule. The exception would allow the FSOC to forego the notice and procedural requirements if it finds that it is necessary to prevent threats posed by a company to the financial stability of the U.S.; such a finding requires a two-thirds vote, including the affirmative vote of the Chairperson.

In this scenario, the FSOC would provide the company with written notice within 24 hours. The company may request an evidentiary hearing within ten days of receiving notice, and the FSOC must hold a hearing within 15 days of receiving the request. A final determination would be announced publicly and subject to judicial review.

Conclusion

The proposed rule and guidance affords some additional insights into the FSOC's approach to SIFI designation, especially the "screens" at Stage 1. The approach presented by the FSOC appears designed to give some firms comfort that they are not likely candidates for designation. Not surprisingly, however, the FSOC's overall approach continues to reserve for itself substantial discretion and flexibility in designating firms as SIFIs.

Given the mid-December comment-period deadline, it seems unlikely that the FSOC will issue a final rule and guidelines until spring 2012. If so, the first designations probably will not take place until summer 2012, a pace that is substantially slower than many had expected when the Dodd-Frank Act was first enacted. That pace may be slowed even further if one or more of the first designees seeks judicial review of a designation, which some observers have suggested is likely. ■

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planning requirement through Section 165(d)(1) of the Dodd-Frank Act. However, the precise contours of what an "acceptable" resolution plan will look like have not yet been firmly established, and additional review of the topic internationally may inform the types of plans that will be acceptable to the Agencies in the U.S.

As to other regulatory frameworks, the U.K. Financial Services Authority (the "FSA"), for example, is moving on a parallel track to the U.S. in implementing its own recovery and resolution planning ("RRP") requirement for U.K.-authorized banks and building societies and FSA-authorized investment firms with total assets of at least £15 billion.[5] Our colleagues in our London office have advised on the U.K. RRP initiative, and although there are significant differences between the U.K. and U.S. approaches, it is important to note two key similarities. First, both the U.S. and U.K. regimes contemplate that the overseas operations of a foreign company will be largely outside the scope of the company's resolution plan. Thus, foreign Covered Companies are not required to give extensive coverage to their foreign operations under the Resolution Plan Rules, and similarly, overseas branches of U.K. entities are not required to prepare an RRP in the U.K. In addition, the U.K. RRP initiative, like the Resolution Plan Rules, contemplates that the FSA will pursue a "phased" approach to implementation of the RRP requirement. After conducting a short initial analysis of submitted RRPs, the FSA will carry out detailed reviews of the RRPs in a phased manner, presumably meaning that RRPs submitted by firms with the highest risk profile will be reviewed first. It seems plausible that the final version of the Resolution Plan Rules, which in their proposed form did not contemplate phased implementation, were influenced by the FSA's phased approach. Regardless, the U.S. and U.K. resolution planning regimes are among the most developed of any national initiatives, are moving at the fastest pace, and promise to have significant implications for other national resolution planning regimes that are less developed.

Separately, the G-20, acting through the Financial Stability Board (the "FSB"), has made commitments to require resolution and recovery plans from all globally systemically important firms. To that end, the FSB has issued several important reports and consultative documents which are likely to impact the resolution planning process at both the international and national level. Most relevant to this discussion, the FSB on November 4, 2011 released a final consultative document on *Key Attributes of Effective Resolution Regimes for Financial Institutions*.[6] We represented the FSR in its participation in a joint trade association comment letter on the FSB consultative document. Our review of the consultative document indicates that U.S. regulators are exercising a powerful influence over the FSB resolution planning initiative, and vice-versa. On October 6, 2011, the FSB issued a consultation paper entitled *Understanding Financial Linkages: A Common Data Template for Global Systemically Important Banks*.[7] Discussed below, the release of this consultative document stands as further evidence that the Agencies envision new data collection and reporting initiatives as an essential component of the resolution planning process. This initiative has accelerated in the U.S., with the Board implementing a new information collection initiative[8] that, although nominally focused on capital planning, is likely to play an important role in the Agencies' efforts to implement the Resolution Plan Rules.

Our recent experiences with the FSB consultative document process and counseling clients on international developments in general have taught us two key lessons about the relationship between national and international resolution planning initiatives. First, the FSB process matters, and its outcome will have (and already has had) a measurable impact on the resolution planning process for Covered Companies. The Board, the Securities and Exchange Commission, and the Department of the Treasury are all members of the FSB, and thus, it comes as no surprise that there are conceptual similarities between the FSB consultative document and the Resolution Plan Rules. Because implementation of the Living Wills Rule has passed from legislative purview to regulatory fiat, there are few, if any "roadblocks" preventing the Agencies from adopting the conclusions of the FSB and other international bodies when implementing the Resolution Plan Rules. Thus, a key takeaway is that Covered Companies should remain engaged, directly and through their trade groups, at the international level.

Second, Covered Companies should *not* expect U.S. and non-U.S. jurisdictions to completely harmonize Resolution Plan Rule requirements.

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At our recent meetings after the Resolution Plan Rules were published, Agency staff starkly asserted that it would be unrealistic as a political matter to assume that the U.S. and other major foreign jurisdictions would be able to fully coordinate resolution plan requirements. Agency staff seemed to conclude that Covered Companies would simply need to accept and address redundant or inconsistent plan terms or requirements across jurisdictions. Similarly, Agency staff indicated they contemplated that a certain amount of information sharing between U.S. and foreign regulators would take place. In this regard, the possibility that information may not be kept confidential by foreign regulators is a matter of concern. Although Agency staff have indicated that they do not intend to engage in wholesale sharing of confidential supervisory information, it must be recognized that once supervisory information is shared with foreign regulators, the chances of the information being made public will increase materially.

Our recent interactions with Agency staff also indicate that the Agencies are diligently seeking to enhance coordination with foreign regulators to the extent they consider practicable. For instance, we recently attended meetings with the Agencies on behalf of the FSR, and at these meetings Agency staff indicated that memoranda of understanding ("MOU") were in place between the FDIC, the Board and "key" foreign regulators, which we take to include the FSA in the U.K. Given that the FSA is still in the process of implementing the U.K.'s own RRP initiative, the existence of such MOUs could affect not only how a Covered Company would be resolved if it were to fail, but also how and to what extent the Agencies would share supervisory information they received from Covered Companies in the course of the resolution planning process. We recommend that Covered Companies monitor the ongoing international regulatory dialogue as closely as possible, and, when advantageous, advocate for MOUs that maintain the confidentiality of supervisory information to the greatest extent possible. As a final note, we recommend that Covered Companies take a pragmatic view, and consider preemptively addressing the strategic implications of, and response to, supervisory information "leakage." Such this leakage could well occur in the next few years as the resolution planning process increases in intensity and scope.

Resolution Plans

What Institutions Are Covered by the Resolution Plan Rules?

The Living Wills Rule covers institutions that fall into one of the following three categories:

1. a nonbank financial company supervised by the Board;

2. a BHC that has $50 billion or more in total consolidated assets, as determined based on the average of the company's four most recent Consolidated Financial Statements for Bank Holding Companies as reported on the Federal Reserve's Form FR Y-9C; or

3. a foreign bank or company that is a BHC or is treated as a BHC under Section 8(a) of the International Banking Act of 1978 and that has $50 billion or more in total consolidated assets, as determined based on the foreign bank's or company's most recent annual or, as applicable, the average of the four most recent quarterly Capital and Asset Reports for Foreign Banking Organizations as reported on the Federal Reserve's Form FR Y-7Q.

An organization that is covered by the Living Wills Rule is deemed to be a "Covered Company." In multi-tiered BHC organizations, only the top-tier BHC will be subject to Covered Company status.

A Covered Company will lose its covered status when it has less than $45 billion in total consolidated assets. This threshold will be calculated as either the average total consolidated assets as reported on the company's four most recent FR Y-9Cs (if the Covered Company is a BHC) or the total consolidated assets as reported on the Covered Company's most recent annual FR Y-7Q, or, as applicable, average total consolidated assets as reported on the Covered Company's four most recent quarterly FR-Y-7Qs (if the Covered Company is foreign). However, as clarified in the preamble to the Living Wills Rule, a Covered Company that loses it covered status would regain it if it again has total consolidated assets of $50 billion or more, as determined based on the most recent annual or, as applicable, the average of the four most recent quarterly reports made to the Board.

An IDI will be covered by the IDI Rule, and thus deemed a CIDI, if it has

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$50 billion or more in total assets, as determined based upon the average of the CIDI's four most recent Reports of Condition and Income or Thrift Financial Reports, as applicable.

When the Resolution Plan Needs to Be Filed

In general, to ease the submission burden on institutions, the Agencies have harmonized to a material extent the various elements of the Resolution Plan Rules (e.g., submission cycle, content, updates, review standards, etc.); however, CIDI requirements under the IDI Rule do differ to some extent from Covered Company requirements under the Living Wills Rule. The following sections highlight at a high level the fundamental requirements of the Resolution Plan Rules and note supplemental learning based on our conversations and meetings with the Agencies' management staff. Before turning to these sections, it is worth noting initially some CIDI-specific elements.

A CIDI's resolution plan is directed to enable the FDIC, as receiver, to resolve the CIDI under the FDI Act in a manner that ensures that depositors receive access to their insured deposits within one business day of the CIDI's failure (two business days, if the failure occurs on a day other than Friday), maximizes the net present value return from the sale or disposition of its assets and minimizes the amount of any loss to be realized by the institution's creditors. As such, the IDI Rule requires that CIDI resolution plans focus on the unwinding and separation strategy of the CIDI, as well as on protection of the deposit franchise and asset disposition strategy. Further, a CIDI's plan must analyze which resolution plan strategy, among several, is the least costly for the FDIC. The industry has expressed to the FDIC how problematic a least-cost resolution analysis would be given its dependence on specific facts and circumstances. Conversations with FDIC staff reveal, however, that such an analysis may be more an ordinal ranking, rather than a detailed analysis under the FDIC's least-cost resolution test. The CIDI framework, thus, is different than the Covered Company one, which seeks an orderly and rapid liquidation pursuant to the Bankruptcy Code and to minimize adverse financial effects to the United States' financial stability.

Submission Cycle

Pursuant to industry feedback during the notice of proposed rulemaking periods, the Agencies have implemented a phased-in approach to resolution plan submissions, based on a Covered Company's (or CIDI's parent's) total nonbank assets (or total U.S. nonbank assets for foreign companies). See chart below.

Total Nonbank Asset Size	Initial Submission Deadline
$250 billion ≤ x	July 1, 2012
$100 billion ≤ x < $250 billion	July 1, 2013
x < $100 billion	December 31, 2013
Post-effective-date covered companies	The next July 1, if that date is at least 270 days after the date the institution becomes a Covered Company or CIDI

Despite this schedule, the Agencies reserve the right to change the initial resolution plan submission dates. Subsequent annual plan submissions would fall upon the anniversaries of the initial plan submission schedule.

Key Resolution Plan Concepts

The content requirements of either the Living Wills Rule or the IDI Rule are based on the following six key concepts, with the first applying to the Living Wills Rule, the second through fifth applying to both rules, and the sixth applying to the IDI Rule.

1. *Rapid and Orderly Resolution* – this concept refers to a reorganization or liquidation of a firm (or U.S. subsidiaries and operations of a foreign firm) under the Bankruptcy Code that can be accomplished in a reasonable period of time in a way that significantly mitigates the risk that failure of the institution would have serious adverse effects on the financial stability of the United States.

2. *Material Financial Distress* – this

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concept means that (i) the firm 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 firm to avoid such depletion; (ii) the assets of the firm are, or are likely to be, less than its obligations to creditors and others; or (iii) the firm 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.

3. *Core Business Lines* – these are business lines, including associated operations, services, functions and support that, in the firm's view, upon failure, would result in a material loss of revenue, profit or franchise value.

4. *Critical Operations* – these are operations of the firm, including associated services, functions and support, the failure or discontinuance of which, in the view of the firm or as jointly directed by the Board and the FDIC, would pose a threat to the financial stability of the United States.

5. *Material Entities* – these are subsidiary or foreign offices of the firm that are significant to the activities of a critical operation or core business line.

6. *Critical Services* – these are services and operations of the CIDI, such as servicing, information technology support and operations, human resources and personnel that are necessary to continue the day-to-day operation of the CIDI.

Our meetings with the Agencies reveal that they intend on meeting with management from each Covered Company whose resolution plans are due on July 1, 2012 to seek greater consistency in these core concepts, and particularly with respect to the critical operations, core business lines, and material entities concepts. These meetings will allow the Agencies to apply greater horizontal consistency in resolution plan review. The Agencies further intend to publish guidance on these concepts that may be helpful to later-round filers.

Neither of the Agencies anticipate bringing enforcement actions for the initial rounds of resolution plan submissions related to content deficiencies. Rather, the Agencies anticipate that the initial submission process will be an iterative and learning one, with each submission round building upon the prior one.

The Living Wills Rule's Filing Requirements Will Vary Depending on the Covered Company's Asset and Country Status

The contents of a Covered Company's resolution plan under the Living Wills Rule will vary depending on whether the firm is domestic or foreign and whether it is eligible for a "tailored" plan or not. As for domestic Covered Companies, resolution plans will incorporate information on the Covered Company's U.S.-domiciled subsidiaries and operations, as well as its foreign subsidiaries, offices, and operations. As for foreign Covered Companies, resolution plans will incorporate information on the foreign Covered Company's subsidiaries, branches and agencies, and critical operations and core business lines that are domiciled in the United States or conducted in whole or material part in the United States. Further, a foreign Covered Company must also (i) describe in detail, and map to legal entities the interconnections and interdependencies among the U.S. subsidiaries, branches and agencies, and critical operations and core business lines of the foreign-based Covered Company and any foreign-based affiliate and (ii) provide a detailed explanation of how resolution planning for the subsidiaries, branches and agencies, and critical operations and core business lines of the foreign-based Covered Company that are domiciled in the United States or conducted in whole or material part in the U.S. is integrated into the foreign-based Covered Company's overall resolution or other contingency planning process.

With respect to asset size, a Covered Company is eligible to submit a "tailored" resolution plan if as of December 31 of the calendar year prior to the date the Covered Company's resolution plan is required to be submitted, (i) the Covered Company has less than $100 billion in total nonbank assets (or total U.S. nonbank assets for a foreign Covered Company), (ii) the Covered Company's total insured depository institutions' assets comprise 85%

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or more of the Covered Company's total consolidated assets (or a foreign Covered Company's U.S. IDI operations, branches and agencies' assets comprise 85% or more of the foreign Covered Company's U.S. total consolidated assets), and (iii) the Covered Company has received prior approval from the Agencies. To obtain approval, a Covered Company must submit to the Agencies written notice of its intent and eligibility to submit a tailored plan at least 270 days prior to its resolution plan submission date. The Agencies may allow for a tailored resolution plan, or may require some or all of the requirements of the full resolution plan.

For each qualifying Covered Company with less than $100 billion of assets, a tailored resolution plan will consist of:

- an executive summary;
- the general information required in the resolution plan but only with respect to the Covered Company's nonbanking material entities and operations; and
- full information on the Covered Company's contacts and interdependencies and interconnections, for both the Covered Company and its IDIs (or U.S. IDIs, branches and agencies for a foreign Covered Company) and nonbank material entities and operations.

Executive Summary

Resolution plans for both Covered Companies and CIDIs must include an executive summary that summarizes the key elements of a firm's strategic plan, material changes from the most recently filed plan, and any actions taken by the firm to improve the effectiveness of the resolution plan to remediate or otherwise mitigate any material weaknesses or impediments to the effective and timely execution of the plan.

Interconnections and Interdependencies

A key component and focus of the resolution plan is the description of interconnections and interdependencies among the Covered Company or CIDI and its material entities and affiliates, and among the critical operations and core business lines of the firm that, if disrupted, would materially affect the funding or operations of the firm, its material entities, or its critical operations or core business lines.

Strategic Analysis

The strategic analysis is a central aspect of the resolution plan and it outlines analytically how the resolution plan can be implemented. The strategic analysis should detail how the Covered Company could be resolved under the Bankruptcy Code or how the CIDI could be strategically separated from its parent and its deposit franchise disposed of. The strategic analysis should include the analytical support for the plan and its key assumptions, including any assumptions made concerning the economic or financial conditions that would be present at the time the firm sought to implement its resolution plan.

Scenarios Analysis

Resolution plans must take into account material financial distress or failure under baseline, adverse and severely adverse economic conditions as provided by the Board. The Board, in coordination with the appropriate primary federal regulatory agencies and the Federal Insurance Office, will conduct annual stress tests of Covered Companies. As part of that exercise, the Board expects to provide Covered Companies with different sets of economic conditions under which the evaluation will be conducted. For its initial submission, a Covered Company or CIDI may submit a plan using only baseline conditions, or if a baseline scenario is not available, a reasonable substitute developed by the firm. The firm also may not rely on the provision of extraordinary support by the United States or any other government to the firm or its subsidiaries to prevent the firm's failure.

Corporate Governance Relating to Resolution Planning

Resolution plans should include a description of how the Covered Company or CIDI has incorporated resolution planning into the firm's corporate governance structure. It should also identify the senior management official who is responsible for overseeing the development, maintenance, implementation and filing of the resolution plan and for the firm's compliance with the Resolution Plan Rules. For the largest and most complex firms, it may be necessary to establish a central planning function that is headed by a senior management official. Such official would report to the Chief Risk Officer or Chief Executive Officer and periodic reports on resolution planning would be made to the firm's board of directors.

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Organizational Structure and Related Information

A Covered Company and CIDI is required to provide detailed descriptions of its organizational structure, unconsolidated financial statements, material liabilities, off-balance sheet exposures, hedging activities, and counterparties, among other items. This information should be mapped to core business lines and critical operations.

Management Information Systems

A Covered Company and CIDI is required to provide information regarding its management information systems ("MIS systems") supporting its core business lines and critical operations, including information regarding the legal ownership of such systems as well as associated software, licenses, or other associated intellectual property. The analysis and practical steps that are identified in this section should address the continued availability of the key management information systems that support core business lines and critical operations both within the United States and in foreign jurisdictions. The resolution plan must also identify the deficiencies, gaps, or weaknesses in those capabilities of the firm's management information systems and describe the actions the firm plans to undertake, including the associated timelines for implementation, to promptly address such deficiencies, gaps, or weaknesses.

Supervisory and Regulatory Information

The Covered Company must identify the relevant supervisory and regulatory entities that have safety and soundness or other supervisory authority over the Covered Company, its material entities, critical operations and core business lines. The Covered Company must also identify foreign authorities responsible for resolving any foreign-based material entity and critical operations or core business lines of the Covered Company. Contact information for the relevant authorities, as well as for the Covered Company, should be provided.

Incorporation of Previously Submitted Resolution Plan Elements

A Covered Company or CIDI may incorporate by reference in its resolution plan information elements (but not strategic analysis or executive summary elements) from prior submissions if clearly identified and accompanied by a certification that the referenced information remains accurate. Our conversations with the Agencies reveal that, to ease the submission burden, a CIDI's resolution plan may simply be a chapter within a larger resolution plan and reference other sections of a Covered Company resolution plan.

Content Exemptions

The Agencies, in the case of a Covered Company, or the FDIC, in the case of a CIDI, may jointly exempt a firm from one or more of the requirements of the Resolution Plan Rules.

Board Approval

Prior to submission of its resolution plan, a Covered Company's or CIDI's board of directors must approve the resolution plan. In the case of a foreign company, a delegee acting under the express authority of the board of directors of the Covered Company must approve the resolution plan. This approval, however, is not an attestation as to the accuracy of the information in the plan, as confirmed by our meetings with the Agencies.

Resolution Plan Review and Enforcement for Deficiencies

Plan Review and Timing

The Agencies have established a review process for resolution plan submissions of both Covered Companies and CIDIs. Generally, the Agencies will preliminarily review plans for completeness within 60 days of receipt, although the IDI Rule does not provide for a specific review period. If the Agencies determine the plan is incomplete (or just the FDIC, in the case of CIDIs), they can request further information. The Covered Company or CIDI will then have 30 days to supplement its plan.

Following their review, if the Agencies jointly determine the resolution plan would not facilitate an orderly resolution, they will notify the firm accordingly in writing and request resubmission of the resolution plan with the deficiencies corrected. Unless otherwise shortened or extended, the firm will have a 90-day window to resubmit a plan with the deficiencies corrected. Throughout the review and information request process, though, the Agencies reserve the right to extend any time frame for review and submission.

Enforcement Remedies

The Resolution Plan Rules provide the Agencies with enforcement powers with respect to the resolution plan review process. If a firm does not adequately remedy Resolution Plan Rule deficiencies identified by the Agencies, for instance, the Agencies may subject the firm to more stringent capital, leverage, or

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liquidity requirements, or restrictions on growth, activities, or operations. Further, if the firm fails, within the two-year period beginning on the date on which the determination to impose such requirements or restrictions was made, to submit a revised resolution plan that adequately remedies the deficiencies, then the Agencies, in consultation with the FSOC, may require the firm to divest itself of assets or operations. Any violation of the Resolution Plan Rules can subject a firm to the Agencies' supervisory enforcement authority under section 8 of the FDI Act.

Notably, as expressed both in the preamble of the Resolution Plan Rules and by the Agencies' staff during our meetings on resolution planning, neither of the Agencies anticipate bringing enforcement actions for the initial rounds of resolution plan submissions related to content deficiencies. Rather, the Agencies anticipate that the initial submission process will be an iterative and learning one, with each submission round building upon the prior one.

Resolution-Based Examination

Although much of the information necessary to assess the credibility of a resolution plan may be obtained through regular examinations, the Resolution Plan Rules provide that firms must provide the Agencies with such information and access to personnel of the firm as the Agencies jointly determine, or as the FDIC determines, in the case of a CIDI, during the period for reviewing the resolution plan, is necessary to assess the credibility of the resolution plan and the ability of the firm to implement the resolution plan.

Interim Notice Requirement

Within 45 days after any event, occurrence, change in conditions or circumstances, or other change that results in, or could reasonably be foreseen to have, a material effect on the resolution plan of a Covered Company (or CIDI), the firm must provide the Agencies (or the FDIC) with notice. The notice must describe the event, occurrence or change and explain why the event, occurrence or change may require changes to the resolution plan. However, a firm is not required to file a notice if the submission date requirement would be within 90 days prior to the date on which the firm is required to file an annual resolution plan. Generally, such notice is not required if an event does not result in, or could not reasonably be foreseen to have, a material effect on the resolution plan of the firm. To be material, the effect on the resolution plan should be of such significance as to render the resolution plan ineffective, in whole or in part, until revisions are made to the plan.

Confidentiality

The Dodd-Frank Act requires the Agencies to "maintain the confidentiality of any data, information, and reports submitted" to them, including resolution plans. The preambles to the Resolution Plan Rules clarify that the Agencies will not provide heightened protections beyond what would otherwise be afforded to a filer under the Freedom of Information Act ("FOIA"). Although FOIA generally provides robust protection for confidential and proprietary business information,[9] Covered Companies and CIDIs need to nevertheless think carefully and strategically about what they include in their resolution plans.

Resolution plans are to be submitted in two sections, one public and one confidential. The public section will be made available to the public and must consist of an executive summary of the resolution plan that describes the business of the firm and includes, to the extent material to an understanding of the firm:

- the names of material entities;
- a description of core business lines;
- consolidated or segment financial information regarding assets, liabilities, capital and major funding sources;
- a description of derivative activities and hedging activities;
- a description of foreign operations;
- the identities of material supervisory authorities;
- the identities of the principal officers;
- a description of the corporate governance structure and processes related to resolution planning;
- a description of material management information systems; and
- a description, at a high level, of the firm's resolution strategy, covering such items as the range of potential purchasers of the firm, its material entities and core business lines.

As recently stated in post-publication meetings with the Agencies, the confidential section will contain other essential information responsive to the resolution planning requirements not otherwise necessary to be put in the public section and that a firm

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otherwise wishes to not have made automatically public. At one meeting we attended with the regulators, agency staff noted that the public section of the resolution plan may be akin to the public section of a bank merger application. A firm that desires confidential treatment of information in the confidential section must file a request for confidential treatment pursuant to the FOIA and the Agencies' respective implementing regulations. Our meetings with the Agencies reveal that such requests will be treated like applications.

The Resolution Plan Rules note that the Board will make plans available to the FSOC upon request. It provides no details as to what level of protection the FSOC, or a subsequent agency will provide to the plans. Similarly, the Agencies have noted in informational meetings that they will provide, to some extent, resolution plans to foreign supervisors, and noted that they could not ensure the confidential treatment of information after distribution to such foreign supervisors. The Agencies plan on having MOUs with key international counterparties that will clarify information-sharing procedures.

No Collateral Legal Effect or Private Right of Action

The Living Wills Rule provides that a Covered Company's resolution plan will not have any binding effect on: (i) a court or trustee in a proceeding commenced under the Bankruptcy Code; (ii) a receiver appointed under Title II of the Dodd-Frank Act (12 U.S.C. § 5381 et seq.); (iii) a bridge financial company chartered pursuant to 12 U.S.C. § 5390(h); or (iv) any other authority that is authorized or required to resolve a Covered Company (including any subsidiary or affiliate thereof) under any other provision of federal, state, or foreign law. The IDI Rule does not have a similar provision, although it clarifies that the FDIC is not bound by the plan.

The Living Wills Rule further provides that nothing in the rule creates or is intended to create a private right of action based on a resolution plan or based on any action taken by the Agencies with respect to any resolution plan.

> Despite the significant costs that Covered Companies will be required to incur, some Covered Companies see certain strategic benefits to the resolution planning process.

Resolution Planning as a Stratergic Tool

Covered Companies will be required to incur significant costs in order to prepare resolution plans. Thus, it is worth asking how the overall process of preparing the resolution plan can be leveraged to benefit the Covered Company itself. As a threshold matter, it is likely that the potential benefit of the process will be positively correlated with a Covered Company's size. The largest Covered Companies (*i.e.*, the companies with the most complexity) have the most to gain from this process, while foreign Covered Companies with a limited U.S. presence have the least to gain, as these Covered Companies have little U.S. presence to address in their plans. Covered Companies that are "in between" these two groups may be able to reap some benefits, depending on how they manage the underlying process. In particular, this middle group of Covered Companies may be able to take advantage of the "learning" which results from interactions between the Agencies and the first group of Covered Companies to file their resolution plans (*i.e.*, Covered Companies with $250 billion or more of nonbank assets). As discussed, the Agencies have indicated that they will distribute a Resolution Plan "template" to the Covered Companies that are required to file their plans by July 31, 2012, and would likely revise this template before distributing it to second- and third-wave filers. Despite the significant costs that Covered Companies will be required to incur, some Covered Companies see certain strategic benefits to the resolution planning process; below, we discuss three of them.

Improving Risk Management Processes

As the Agencies indicated in meetings with us, the overriding objective of the Resolution Plan Rules is for Covered Companies to "demonstrate resolvability," both to the Agencies themselves and to the market as a whole. The requirement that Covered Companies "demonstrate resolvability" can be understood in two different ways. First, this requirement can be understood to impose a substantive requirement that a Covered Company to draft a resolution plan which demonstrates that the Company is *structurally* resolvable in the event of its material

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financial distress. Thus, the Resolution Plan Rules contain provisions requiring a Covered Company to disclose the structural relationships between entities in its overall group. Meeting this first plan requirement may require the development of more comprehensive MIS systems, as discussed in more detail below.

Second, this requirement can be understood to impose an implicit (but no less important) obligation on the Covered Company to demonstrate that its analytical processes are sufficiently robust to ensure that it can be successfully resolved. In other words, the Resolution Plan Rules require a Covered Company to demonstrate to the satisfaction of the Agencies that its management is thinking about resolution in the right way. In this regard, it is no surprise that the most important element of a Company's resolution plan is the "strategic analysis" portion, which requires a Covered Company to in essence lay out its strategic thinking about resolution. Our meetings with Agency staff indicate that they are emphasizing this requirement, and are seeking to gauge how Covered Company management are thinking about resolution planning at the very highest levels. By forcing Covered Companies to engage in a gamut of strategic stress testing and scenario analyses, the Resolution Plan Rules may give Covered Company management no choice but to engage in exactly the type of downside planning which some recommend that financial institutions engage in anyway.[10] Because of this, Covered Companies may seek to leverage the power of these required mental exercises to re-think, and perhaps improve, their strategic thinking about resolution.

Self-Assessing "Criticality"

The Resolution Plan Rules require Covered Companies to provide the Agencies with a strategic analysis relating to their "material entities," "critical operations" and "core business lines." There is, of course, a lack of uniform agreement among Covered Companies about which entities are "critical" for purposes of this analysis. The Agencies recognize this lack of uniformity and, as discussed, indicated in recent meetings that they would seek to ensure that the Covered Companies whose plans are due July 31, 2012 consistently define material entities, core business lines and critical operations. In addition, FDIC staff indicated at our recent meeting that they intend to disclose certain elements of their approach to developing "OLA Resolution Plans," resolution plans which the FDIC would implement in the event that a Covered Company were subject to orderly liquidation under Title II of the Dodd-Frank Act. Taken together, these two initiatives can be understood as a dialogue between the Agencies and Covered Companies about how best to assess the systemic significance of the various entities within Covered Companies' overall groups.

We understand that some Covered Companies are seeking to leverage this process to examine their own assumptions and strategic thinking about which of their affiliates or subsidiaries are indeed "critical" to their survival. They are engaging in robust self-analysis about how they assess "criticality," and are determining if their assumptions about which entities are critical and which are not can withstand Agency scrutiny. This dialogue could help a Covered Company clarify its strategic thinking about its most essential operations.

MIS System Enhancement and Modernization

It is important to remember that the resolution planning initiative, both at the U.S. and international level, places a heavy emphasis on a company's ability to deliver comprehensive, high quality information about its activities, risk profile and exposures on a consolidated basis. As noted, this emphasis has most recently manifested itself in an FSB consultation paper, *Understanding Financial Linkages: A Common Data Template for Systemically Important Banks.* The consultation paper, which proposes a comprehensive new framework for collecting financial data from systemically important banks, emphasizes that "in the recent crisis, the lack of timely, accurate information has proved very costly," and the current financial data architecture "lags well behind the forces driving increased complexity and globalization of financial systems, institutions and markets." With respect to the Resolution Plan Rules, this emphasis has manifested itself in provisions of the Resolution Plan Rules requiring Covered Companies to submit detailed inventories of their MIS systems, including, *inter alia*, detailed inventories and descriptions of key MIS systems and applications, including systems for risk management, accounting and financial and regulatory reporting.

These provisions of the Resolution

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Plan Rules offer the Agencies an opportunity to "grade" a Covered Company's MIS systems, and the Agencies will likely take full advantage of this opportunity. Importantly, this grading process will allow the Agencies to do an "apples to apples" comparison between and among the MIS system capabilities of the Covered Companies, as MIS system capability would seem to be much more capable of "objective" assessment than, for example, the strategic analysis portion of a resolution plan. Because the Agencies are likely to focus on the quality of a Covered Company's MIS systems, some Covered Companies have recognized that such an initiative could have significant benefits separate and apart from the resolution planning process. First, there are obvious ancillary business benefits to streamlined MIS systems. Recent media reports indicate that large banking organizations are seeking to streamline their MIS systems simply because it makes sense from a cost perspective.[11] Second, a Covered Company is best equipped to manage risk (regulatory risk included) on a consolidated basis if its MIS systems are streamlined. The Agencies, the Board especially, continually seek information about the consolidated risk profile of the companies they regulate; and thus a Covered Company with the ability to quickly marshal and present consolidated data about itself will be well-equipped to respond to Agency requests for information about its financial position and risk-management capabilities. In sum, Covered Companies are looking at the resolution planning process as an opportunity to streamline and right-size their MIS systems infrastructure, and in so doing improve their risk management capabilities and establish competitive advantage.

Conclusion

Without a doubt, the Resolution Plan Rules will impose significant costs on Covered Companies and CIDIs. For most firms, the process of building the MIS systems infrastructure necessary to comply with the Resolution Plan Rules has yet to begin in earnest, nor has the actual process of plan drafting. In order to emerge unscathed, Covered Companies and CIDIs will need to manage the process with skill and finesse, both with respect to the internal processes of project management, strategic analysis, and plan drafting, and with respect to the external processes of interacting with the Agencies and foreign regulators. We are well-positioned to remain abreast of statutory, regulatory and supervisory developments that will influence implementation of the Resolution Plan Rules, and we will continue to keep our clients informed as the resolution process continues, both in the U.S. and abroad. ■

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1. 76 Fed Reg .67323 (Nov. 1, 2011).
2. FDIC, *Resolution Plans Required for Insured Depository Institutions With $50 Billion or More in Total Assets*, 76 Fed. Reg. 58,379 (Sept. 21, 2011), available at http://www.gpo.gov/fdsys/pkg/FR-2011-09-21/pdf/2011-24179.pdf.
3. *See* 12 U.S.C. § 1819(a) (rule-writing authority under the FDI Act); 12 U.S.C. § 1821(d)(1) (governing the operations of FDIC receiverships); 12 U.S.C. § 1820(b)(3) (information collection authority to conduct examinations of insured depository institutions ("IDIs")).
4. *See* Memo to FDIC Board, *Resolution Plans Required for Insured Depository Institutions with $50 Billion or More in Total Assets – Interim Final Rule* (Sept. 9, 2011) (citing calls from G-20 leaders), *available at* http://www.fdic.gov/news/board/Sept13no5.pdf.
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8. Capital Plans; Proposed Agency Information Collection Activities: Comment Request, 76 Fed. Reg. 55,288 (Sept. 7, 2011), *available at* http://www.federalreserve.gov/reportforms/formsreview/Regs_GOWBBLLMM_20110913_ifr.pdf.
9. *See* 5 U.S.C. § 552(b)(4).
10. *See, e.g.*, Oliver Wyman, *The Financial Crisis of 2015: An Avoidable History* (recommending that financial institutions engage in "downside" scenario planning), *available at* http://www.oliverwyman.com/3697.htm.
11. *See, e.g.*, CNBC, *Inside Citigroup's Strategy to Become Global Consumer Bank* (Jan. 24, 2011), *available at* http://www.cnbc.com/id/41233935/Inside_Citigroup_s_Strategy_to_Become_Global_Consumer_Bank.