FEDERAL DEPOSIT INSURANCE CORPORATION

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SYSTEMIC RESOLUTION ADVISORY COMMITTEE

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MEETING

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WEDNESDAY,
NOVEMBER 9, 2022

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The Advisory Committee convened at 9:00 a.m. EDT in the Federal Deposit Insurance Corporation Board Room at 550 17th Street NW, Washington, DC, Martin J. Gruenberg, Acting Chairman, presiding.

PRESENT:
SHEILA BAIR, Former Chairman, Federal Deposit Insurance Corporation*
SHELLEY C. CHAPMAN, Senior Counsel, Willkie Farr & Gallagher, Former United States Bankruptcy Judge, Southern District of New York*
TIM P. CLARK, Distinguished Senior Banking Advisor, Better Markets, Former Deputy Director of Supervision and Regulation, Federal Reserve Board of Governors
JAY CLAYTON, Former Chairman, U.S. Securities and Exchange Commission (SEC)
H. RODGIN COHEN, Senior Chairman, Sullivan & Cromwell LLP
GARY COHN, Former Assistant to the President Economic Policy and Director of the National Economic Council
ROBERT DRAIN, United States Bankruptcy Judge, Southern District of New York

D. WILSON ERVIN, Former Vice Chairman, Credit Suisse
RICHARD J. HERRING, Co-Director, The Wharton Financial Institutions Center 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, DTCC, President and Chief Executive Officer of DTC, FICC and NCSS
TIMOTHY J. MAYOPOULOS, President of Blend, Former President and Chief Executive Officer of Fannie Mae
SANDIE O'CONNOR, Former Chief Regulatory Affairs Officer, JPMorgan Chase & Co.
DOUGLAS L. PETERSON, President and Chief Executive Officer, S&P Global
JOHN S. REED, Former Chairman and CEO of Citigroup and Former Chairman, Corporation of Massachusetts Institute of Technology
MEG E. TAHYAR, Partner and Co-head of Financial Institutions, Davis Polk LLP

ALSO PRESENT:

MARTIN J. GRUENBERG, Director, Federal Deposit Insurance Corporation, Acting Chairman
ROHIT CHOPRA, Director, Consumer Financial Protection Bureau
MICHAEL J. HSU, Acting Comptroller of the Currency
ELKE K™NIG, Chair, Single Resolution Board, European Union
JON CUNLIFFE, Deputy Governor for Financial Stability, Bank of England*
SUSAN BAKER, Division of Complex Institution Supervision and Resolution
JOHN P. CONNEELY, Director, Division of Complex Institution Supervision and Resolution
ELIZABETH FALLOON, Office of General Counsel
ANDREW FELTON, Deputy Director, Systemic Risk
JAMES (JIM) MCGRAW, Senior Deputy Director, Division of Complex Institution Supervision and Resolution
ARTHUR J. MURTON, Deputy to the Chairman for Financial Stability
ALFRED SEIVOLD, Deputy Director, Institution Risk, CISR
R. PENFIELD STARKE, Senior Counsel. Legal Division
RYAN TETRICK, Deputy Director, Resolution Readiness, Division of Complex Institution Supervision and Resolution
JENNY TRAILLE, Division of Complex Institution Supervision and Resolution
DAVID WALL, Deputy General Counsel (Acting), Resolution and Receivership Branch

*Present via video teleconference

C-O-N-T-E-N-T-S

P-R-O-C-E-E-D-I-N-G-S

9:04 a.m.

ACTING CHAIRMAN GRUENBERG: Well, good morning, everybody. Welcome to the FDIC. We haven't seen you all for a while. So it's nice to be together.

I actually checked the calendar. The last time this committee met virtually was in October of 2020. And the last thing this committee met in person hard to believe was December of 2018. So it's been four years since we've actually seen you all.

And we're going to do our best not to let another four years pass without seeing you again. And we're going to try to resume annual meetings of this committee which really has enormous value to us in an area that is of vital importance to the FDIC. At the end of the day, our ability to manage the orderly failure of a systemic financial institution is probably -- will probably be the ultimate credibility test for our agency.

And how our agency is viewed will be determined by how we handle that challenge. And our preparations to carry out that responsibility are absolutely central to what we do. And our ability to meet with you on a regular basis to share with you the work we're doing and to get your input really has enormous value too.

So we thank you for being here. And so it's a large committee. It may get larger. So we're a little bit cramped, but I hope you bear with us. We wanted to take advantage. Let me begin by introducing some of the new members who have joined up, Tim Clark who is the distinguished senior banking advisor of Better Markets. And some of you may know him as the former deputy director of Supervision and Regulation at the Federal Reserve.

Tim was definitely a partner in crime with us. It was really our partnership with the Tim and the Fed that allowed us to make the Title I resolution plans into meaningful tools for us to use to enhance the resolvability or largest, most systemic global financial institution. So the fact that we were able to entice Tim to join this committee was a big plus for us.

And let me also introduce Frank La Salla, the president and CEO of the Depository Trust Clearing Corporation, DTCC. One of our top priorities at the FDIC and it's an international priority as well is making progress on the resolution of central clearing counter-parties. They in some ways define what systemic risk is.

And in all the areas in post-crisis resolution, I think it's arguable that we've made the least progress in regard to CCP resolution. So that is a top priority for us here at the FDIC and domestically here in the United States. And it's a major priority internationally for the Financial Stability Board. And we're going to have a discussion around that later this morning.

In addition, we've been joined by several other distinguished new members. This will be their first meeting, Jay Clayton, the former chairman of the Securities and Exchange

Commission, Margaret Tahyar, partner and co-head of financial institutions at Davis Polk, and Wilson Ervin, former vice chairman at Credit Suisse who played a formative role in helping define thinking around the issue of systemic resolution. And if I may introduce a special guest who's joining us this morning, Elke K”nig who many of you may know she is the chair of the Single Resolution Board for Europe.

Elke is the founding chair of the Single Resolution Board. There was no resolution authority in Europe before Elke. And there is now a viable, robust institution, really the first institution of its kind in the European community with a capacity for resolving large financial institutions.

Elke is finishing her second term as chair next month. And she'll be required to set down the limit of her service. And she's graciously agreed to join this committee after she steps down as chair of the SRB. She'll be an invaluable addition to us.

And let me recognize if I may four former members whose terms expired and have left the committee, Bill Donaldson, former chair of the SEC, Peter Fisher, former Undersecretary of the Treasury and now a senior fellow with the Tuck School of Business at Dartmouth, Gary Stern, former president and CEO with the Minneapolis Fed, and Michael Bodson, president and CEO of DTCC. And we now have the benefit of his successor serving on the committee. We have a full agenda, so I'm not going to take more time.

But we've really broken the morning into three sessions that I think will be of interest to you. The first session is going to focus on our efforts to integrate our supervision and resolution responsibilities. I think one of the strengths of the FDIC is we have in one institution responsibility for resolution, a significant part of supervisory responsibility in the U.S. banking system as well as the deposit insurance responsibility.

Tremendous synergies among those three

functions and the importance of close collaboration and integration between supervision and resolution is really fundamental to an effective resolution process. We want to talk about our work from that perspective. In the second session, we're going to focus on our two key resolution priorities, our ongoing work for systemic resolution under Title II of the Dodd-Frank Act and our utilization of the orderly liquidation authority.

And we're going to focus in particular on our work around increasing transparency and how we think about Title II resolution and communicating with financial markets as well as the public to try to establish better understanding of what we do. And that is really not a simple task as you all probably understand better than most. So we want to talk about that issue.

And then also what is a key priority for us which is enhancing our ability to manage the failure of large banking organizations below the GSIB level. It's really a very distinct resolution challenge for us from the GSIBs in many ways as great as the GSIB challenge. And because we were so obsessed with developing a capability to manage the failure of GSIBs, that was not the first thing we turned to was not the large banks.

And then we woke up and realized the failure of one of these large banking institutions could really be an enormous challenge with financial stability implications. So we devoted a lot of time. That's a priority I think for all three of the U.S. banking agencies, the Fed, and the OCC as well as the FDIC.

And as you may know, the FDIC and the Fed issued a joint advanced notice of proposed rulemaking to see public comment and the possibility of establishing a long-term debt requirement for our largest banking organizations below the GSIB level to facilitate a capacity for orderly failure. So we'll talk about all of that work. And then finally, we're going to have a session on the issue I mentioned previously, the challenges relating to the resolution of a central counter party.

Central counter parties as you all well know were a systemic consequence before the 2008 crisis. And then as a result of one of the key reforms after the crisis of mandating clearing for derivatives, it anything, we expanded the systemic footprint of CCPs. And it's not clear that the resolution capacities here in the United States or internationally really evolved to deal with the enhanced systemic risk that a failure of a CCP could present.

So we've been spending a lot of time on that here at the FDIC. It's a big priority and focus of attention internationally within the Financial Stability Board and within other jurisdictions. So we're going to continue that discussion here, and we have a special guest joining us virtually who some of you may know, Sir Jon Cunliffe who's the Deputy Government of the Bank of England for financial stability.

And Jon is also chairing the committee on payments and market infrastructure of the BIS. He's been focused on payment issues internationally and in particular the supervision and resolution of CCPs. He's really been an international leader on this issue, and we thought we could benefit from a conversation with Jon.

So that's our program for this morning. Thank you all for being here. We have the privilege of being joined by our other Board members, acting controller Mike Hsu and director of our Consumer Financial Protection Board -- Bureau -- it's still early in the morning I got to tell you -- Rohit Chopra. Mike, would you have any comments?

DIRECTOR HSU: Just to say it's great to be here to see a lot of familiar faces, to meet some new folks. These issues are very near and dear to my heart. So I just look forward to jumping right in. Thank you.

ACTING CHAIRMAN GRUENBERG: In his

previously life, Mike was also a partner in crime with Tim Clark over at the Fed.

DIRECTOR CHOPRA: Partner in compliance.

(Laughter.)

DIRECTOR CHOPRA: Well, let me just thank all of you for being here. And I want to echo it's good to be with people in person again. The staff has prepared a lot to make sure that they can solicit feedback from all of you.

I'm just going to echo a couple of things that the acting chairman discussed that are issues of concern for the Board, for me, for others. And as Marty mentioned, obviously the failure of a domestic systemically important financial institution would be quite challenging. The FDIC has some good experiences, bad experiences, and learning from this. And I think it's no surprise that a CFPB director is worried about the failure of an institution with an enormous footprint in consumer and retail banking, a very large number of accounts and the regional impact or national impact of its failure.

And I think as he mentioned, there has been a proposal, an ANPR by the FDIC and the Fed about ways to prevent that and remove from the play book of simply selling it to a GSIB. I'll also add a couple of other points of concern for me. One is obviously the undesignated non-bank systemically important financial institutions.

The Financial Stability Oversight Council has not designated any in quite some time. And I think many experts agree they exist. And we do not have resolution plans for them. That would make resolution very challenging and create an enormous amount of complexity.

And of course, the work that the acting chairman has mentioned about the GSIBs, there's no victory to be declared. There are still a number of complexities that of course U.S. law requires us to evaluate those resolution plans based on whether they can be credibly completed in a Chapter 11 bankruptcy which I think many of us know is a fairytale right now. So there's so much work I think we need to do. The markets have obviously changed quite a bit since the last time you met together. So really looking forward to the discussion.

ACTING CHAIRMAN GRUENBERG: Thank you, Rohit. Let me turn the program over to John Conneely, the Director of the FDIC's Division of Complex Institution Supervision and Resolution. John?

MR. CONNEELY: Thank you, Chairman Gruenberg. Good morning and thank you all for joining us today. I am John Conneely, the Director, as Marty said, of the Division of Complex Institution Supervision and Resolution, although it's much easier to say CISR. So we'll stick with that.

I'm joined at the table by the panelist for our first session, Senior Deputy Director Jim McGraw, Deputy Directors Andy Felton and Alfred Seivold, and our legal counsel, David Wall. Before we get started, I just unfortunately need to take care of a couple of administrative matters. First, our legal staff has asked I provide two statements for today's meeting.

The first is a statement regarding the Sunshine Act. So I'll read that. We have all members of the FDIC Board of Directors in attendance today as we begin the advisory committee meeting.

The government in the Sunshine Act imposes notice and access requirements whenever a quorum of the FDIC's Board of Directors meets to conduct or determine agency business. This meeting is not held for such purposes and does not constitute a meeting under the Act. The Board members present will only engage in general or preliminary discussions that do not relate to specific proposals for action pending before the FDIC.

Any specific issues for official Board resolution remain open for full consideration by the Board following the conclusion of the meeting. The second statement -- excuse me -- regards the advanced notice of proposed rulemaking, or ANPR which was mentioned, concerning potential new resolution related resource requirements for large banking organizations which was approved by the FDIC Board of Directors on October 18th, 2022 and also approved by the Board of Governors of the Federal Reserve System and is currently open for comment. Staff will not respond substantively to any comments on the ANPR and generally will be in listening mode and not indicate the direction the agencies are likely to take with respect to NPR or Final Rule.

In addition per our regular practice, the FDIC will publish a summary of this meeting relating to the ANPR on our public website. The summary will generally include a list of participants and a high level summary of the discussion. And if you have questions on either of those statements, we have our FDIC legal staff who would be happy to answer.

(Laughter.)

MR. CONNEELY: Just a couple of technical notes, if you'd like to speak, just press the green lights on your microphone. Or for those who will be participating remotely, you can use the Webex raise hand function. But there's really no need to be so formal.

And in the meeting, please jump into the discussion at any time. I'm sure people are not shy here. So I'd also like to remind participants that the meeting is public and is being livestreamed.

So I appreciate the opportunity to provide a few introductory comments today. And today we'd like to provide the committee with an update on work being done with respect to systemic resolution along with some of the challenges that we continue to face. And we look forward to the committee's input to help further our work in these matters.

And so let me just take a minute to set the stage for today, particularly for new members. As you know following the 2008 financial crisis, Congress established new authorities for the FDIC to manage the orderly resolution of large complex financial institutions whose failure could threaten U.S. financial stability, most notably Titles I and II of the Dodd-Frank Act. Shortly thereafter in June 2011, then FDIC chairman Sheila Bair convened the first meeting of this committee, noting that the knowledge and expertise brought to bear by members of the committee would greatly enhance the corporation's efforts to develop and implement these tools.

In the seven meetings held since then, a wide range of systemic resolution issues have been brought to the committee in order to test thinking and solicit your feedback. The first meetings obviously focused on core aspects of the systemic resolution, including the establishment of the orderly liquidation authority and the development of the foundational single point of entry strategy. Subsequent meetings discussed various structural reforms to operationalize the SPOE strategy such as long-term debt -- requirements for long-term debt, clean holding companies, orderly transfer of QFCs.

And more recently, the committee has discussed their work on cross border engagement, bankruptcy challenges, Title I reviews, capabilities testing which we'll hear a little bit about today, broker-dealers, and other developments. And thanks to the input from you all on these issues. The FDIC has really made significant strides in systemic resolution planning.

Yet challenges remain which brings us to the agenda for today. And I know Chairman Gruenberg went through some of the agenda. I just want to elaborate on a couple of points, and I'll just walk through. And on Slide 4, we have the agenda.

The first session really will be just a brief update by risk staff on recent work in CISR to integrate supervisory and resolution responsibilities. I'm sure many of you remember during the financial crisis the coordination challenges that we faced between the agencies, between supervision and resolution. And a lot of work has been done since then to bridge these gaps.

And we look forward to your thoughts on the directions we're taking here in CISR in that regard. So as Jim and Andy and Alfred go through their presentations, we'd like you to think about your experiences and the challenges you've faced and share them and maybe identify ways that we could do this better. The second session which is really the heart of the meeting today, our resolution staff will discuss two topics, GSIB resolution planning under Title II and the need for public transparency and the challenges and options for resolving non-GSIB large banks.

Here as the chairman mentioned, we'll introduce and discuss the topic of transparency. The FDIC has a long record of fostering public confidence. Everybody knows if you walk into the bank and see that FDIC sign, your deposits are safe.

And we really want to build on that level of confidence around the execution of our Title II authorities. In essence, what we're looking for from you is who needs to know what and when about our efforts to help build our credibility and confidence. The second topic, the resolution of large banks that are not GSIBs is new for consideration by the committee.

In this session, we'll seek your input about the work we're doing and the challenges this work presents which are formidable, whether it's for the FDIC or the financial system. And then the third session as mentioned, we returned to a topic that we briefly discussed with the committee in 2020 which is the challenge of resolution of CCPs. This topic is one that is on a lot of policy makers' minds globally and a lot of work is being done and warrants continued consideration by the committee.

And we look forward to hearing from our guest speaker, Sir Jon Cunliffe, and from you all on how we should go about being prepared and prioritize these challenges that we have. Are there any questions on the agenda before I move on? No? Okay.

So then as a kickoff to our first session, let me just -- which is on the integration of supervision resolution, let me just take a couple minutes to reintroduce CISR which is the division primarily responsible for executing the FDIC's supervision and resolution responsibilities for the largest and most complex financial institutions. You'll see on slide 3 the mission of CISR. And it's pretty straightforward: to protect and maintain stability in the U.S. financial system by avoiding and if necessary managing the failure of a large complex financial institution.

So this mission statement clearly sets out a focus on the use of both supervisory and resolution authorities to address financial stability. And the focus and approach really has been driven by the evolution of the banking industry. The growth over the past 35 years and the actual and relative size and the result and complexity of the nations' largest banks along with the broadened systemic resolution powers that have been provided under Dodd-Frank really has caused the FDIC over time to adopt new and more sophisticated approaches to its supervision, resolution, and insurance functions.

The changes were naturally incremental. And over time, the FDIC had specialized staff working on very similar issues throughout the organization. There were a lot of challenges in coordination. Supervisors don't like to talk a lot about failure. And resolution specialists like to talk about nothing but failure.

(Laughter.)

MR. CONNEELY: So we had a bridge that we needed to cross and bring together. So an important part of this evolution was the creation in 2019 of CISR really to consolidate all those resources and adopt a more integrated approach that leverages both our supervisory and resolution responsibilities. As the need to plan for the resolution of these institutions starts long before the stresses begin.

We have to start well into BAU. So we work, CISR works proactively early on to fully understand the firm's unique characteristics and activities, the degree of complexity, their resiliency, very important on the resiliency, the level of risk, and the their potential impact on financial stability. And to accomplish this, we build cross disciplinary teams that integrate professionals throughout the division: resolution, supervision, lawyers, economists, pretty much anything you can think of.

And we work also closely with our other divisions and our sister agencies. And we've done a lot of work -- a lot of good work with the OCC and the Fed on this typic. We also engage in active cross border coordination through our work of our supervisory colleges and crisis management groups which really are now part of our BAU activities to build and maintain our readiness.

And we had both, the supervisory colleges and the crisis management groups, which are looking at the same institutions from two different perspectives. And we look at them with staff from both sides. So in taking this approach, we're hoping to achieve several overarching objectives.

One is to improve our coordination, our consistency, and our accountability. Secondly is to foster a collaborative and interdisciplinary approach to these issues. And third and really most importantly, we want to insure the information, resources, and expertise are shared in advance and readily available in the event of a crisis situation. So with that, I will turn -- well, I'll just stop for a moment if anybody has any questions before I move on.

(No audible response.)

MR. CONNEELY: Okay, great. So then I will turn it over to Jim McGraw. He will expand on our efforts to better integrate supervision and resolution. Thank you.

MR. MCGRAW: Thanks, John. So good morning and welcome to the advisory committee members and the guests here in the room and those who are joining us online. My name is Jim McGraw. I'm the senior deputy director of the FDIC's Division of Complex Institution Supervision Resolution or as I will refer to it going forward, as John said, CISR.

So this morning, I'm going to briefly discuss the unique organizational structure within CISR where we have brought together within one division the supervision or risk expertise and the resolution expertise. The communication, the collaboration, the cooperation, sharing of information, sharing of expertise between supervision and resolution within CISR really is one of the fundamental benefits of having both disciplines in one division. So within CISR, we have three business line branches.

We have institution risk, systemic risk, and resolution readiness. We also have a fourth branch, the operations branch which supports the other three business line branches. Institution risk provides our firm specific onsite supervisory work focusing in on key risk vulnerabilities, resiliency, the adequacy of risk management practices within the firm.

Systemic risk is focused on systemic and emerging risks within our portfolio firms and looking at it more horizontally across the firms and then also look at those risks within the financial industry itself. Also systemic risk is responsible for supporting our supervisory programs, for developing and monitoring policy, developing our quantitative analytical tools. There's a lot of information that comes in, a lot of data from these firms and there's a lot of analytical tools that we build out to help us in both our risk and our resolution work.

And they also oversee our

international coordination which I'll talk about in a little more detail in a few minutes. And then we've got the resolution readiness branch which formulates in the event of a failure would be responsible for leading the execution of a strategy to resolve a large complex financial institution, either under the FDI Act or Title II of the Dodd-Frank Act. The flow of information and analysis between these branches is critical.

Knowing where the key risks and vulnerabilities and risk management weaknesses exist within specific business lines, material entities, critical services, critical operations. Where those are located within the firm, understanding the interconnectedness within the firm, ultimately understanding where a firm stands on the crisis continuum from a risk perspective is critical in determining where resolution readiness resources need to be focused. And also knowing the information needs on the resolution readiness side helps inform our supervision side when they're prioritizing and developing their supervisory plans.

But the risk and readiness branches, we have regular structured discussions. We have ad hoc discussions. We have information sharing programs.

We have an interdivisional committee made up of executive managers from all three branches that meets to oversee and ensure that we have appropriate supervisory and resolution strategies in place that complement each other. Within CISR, we have an escalation protocol process which is a collaborative process between risk and readiness where firms are evaluated and placed into priority focus buckets based on risk profile perceived probability of default. And then that is able to serve as a guide as we develop steps that can be taken to better prepare for a potential resolution of that.

I mentioned the international coordination within the systemic risk branch. The crisis management groups John mentioned, CMGs, are a significant part of that coordination. They exist to facilitate cross border cooperation among both supervisory and resolution authorities, representing home and host jurisdictions for the systemically important financial institutions.

We have firm specific information sharing and cooperation arrangements that support this cross boarder crisis planning activity. And then the members maintain regular dialogue. We have formal generally on an annual basis meetings where we build and maintain relationships between the different authorities, exchanging information relevant to resolution planning to ensure that we have a rapid resolution response in a time of stress.

I'll also mention that the CMGs have really enhanced our internal CISR coordination between all the branches as over the last couple of years all of the disciplines, risk and supervision, have worked together in planning and preparing for these CMG meetings. And bringing the onsite supervisory perspective into these meetings has really enhanced their effectiveness from a resolution planning standpoint. Cyber risk, I'm just going to mention this quick.

It's just an example of a risk where the coordination and communication between supervision and resolution is key. Understanding where cyber risk vulnerabilities are within the firm, within the business lines, material entities how it could impact different critical services, critical operations is key when assessing and planning for resolution risk. Slide 7. I'll mention for Title I Planning.

Again, the presence of our onsite supervisory staff monitoring the condition and the risk management of large complex financial institutions, the knowledge gained through examination participation and in our offsite analysis, it's a valuable resource that we have to leverage as part of the Title I plan review process. Onsite supervisory staff have access to specific information that can supplement the information that the firms provide in their Title

I plans and should be incorporated into our overall plan assessment. Information learned through supervisory programs can be critical in understanding a firm's Title I capabilities which, in turn, informs from a Title II perspective as well.

Supervisory programs should be used to help us to test assumptions and capabilities and assertions that firms put within their Title I plans. I'll point out the drafters of original 165(d) rule actually recognize the value of incorporating supervisory programs into Title I plan review where it states in the rule that the Board and the corporation will rely to the fullest extent possible on examinations conducted by or on behalf of the appropriate federal banking agency for the relevant company. Related to recovery plans, CISR staff from both resolution readiness and risk have been working closely with the other banking agencies to plan for and participate in in-depth reviews of recovery plans submitted by firms subject to the

OCC's recovery plan rule.

And again, this work has considerable overlap with Title I and Title II. Finally, I do want to note and this has already been mentioned by Chairman Gruenberg and by John. But my comments up to this point have focused on banks and bank holding companies where we have the supervisory insight and the Title I work that we're able to use that to support a robust resolution preparation for those institutions.

However, we also have responsibility for resolving nonbank financial companies if their failure threatens U.S. financial stability. And the work associated with the nonbank financial companies is more difficult given we don't have nearly the same resolution tools or resolution engagement and insight with those firms. A common challenge that we discussed with you back in 2020 was the fact that the FDIC didn't have access to certain data that would be needed in the runup to or during a resolution event for one of these companies.

Another more specific challenge which Jenny Traille will talk about later this morning is the fact that the nonbank financial companies are not required to submit Title I resolution plans. And as we've mentioned, Title I plans provide the FDIC with direct access to key information that would be useful in supporting a Title II resolution. So to address those impediments to nonbank financial company resolution planning, we do work closely with the other regulatory agencies, both domestically and internationally, to help sharpen our understanding what the FDIC might need to undertake a successful resolution of one of these firms.

We've also put in place data sharing arrangements for the FDIC to receive material nonpublic information from the firm supervisors. But I will say even with the best efforts, it's still difficult to address the root challenges that we face in thinking about a Title II resolution of a nonbank financial company. And again, we devoted a whole segment on the agenda to CCPs later this morning where I'm sure we'll have a very robust discussion on that topic. So with that, I'll stop and just open it up if anyone has any questions or comments. Yes, John.

MEMBER REED: Jim, impressive how you're coordinating all of this yourselves. What about the interaction with the institutions themselves? Obviously, supervision can be pretty formal. Do you have informal sort of interactions with the targeted companies themselves that would allow you to flesh some of your work and their sort of response to it? Because to some extent, you're part of their immune system.

MR. MCGRAW: I mean, on the supervisory side, we have daily --

MEMBER REED: Sure.

MR. MCGRAW: -- contact with our onsite presence. Through the CMGs, we have access and discuss the resolution topics with the firms during those meetings. And then during the recovery plan review work, we'll have discussions with the firms there. On Title I, we have discussions with the firms. So we are able to build into a lot of our interaction with the firms, the resolution issues and concerns that we might have.

MEMBER REED: So there isn't a barrier that's making your job harder?

MR. MCGRAW: I would say that the whole purpose behind the formation of CISR was to break down that barrier. And I think we've done a good job getting that in place. There's still more work to be done. But the integration of the supervision and resolution is much stronger now than prior to the formation of CISR.

MEMBER ERVIN: A question that goes back to something that John mentioned. I used to run a credit department in a former life. And one of the tensions was how to deal with the credit officers who thought the credit was good and would sometimes fall in love with it as it's going down to a difficult path.

And how do you discover that dance of when to turn to recovery? You don't want to move too early. But you also don't want to be too late. So as you've integrated these two teams, how do you deal with that issue to make sure that people don't fall in love and think of this as a black mark if I turn it over to resolution, I failed as a supervisor?

MR. MCGRAW: I think that's a really good question. And I would say and others can chime in too. I would say the formation of CISR, we've tried to -- that's been one of the purposes of that is to bring them together where we're not thinking this as, okay, this all belongs to supervision.

And now -- oh, now we got to turn it over to resolution. We're all one team working on this together. And the development when I mentioned the escalation protocols, that's work that's done collaboratively between supervision and resolution where we're looking at firms and we're discussing the risk profile of the firm.

How well is the risk being managed? What is a perceived probability of default on that firm? And we have a lot of really honest, frank discussions in those committee meetings as far as where should firms be placed within these priority risk buckets.

And so I would say our conversations on a daily are integrating both supervision and resolution. And we've hopefully done a good job getting rid of -- it belongs to the supervisory side until everything has already hit the fan and now we're heading it over to resolution.

MR. CONNEELY: Yeah, I'll just add that really is an excellent question. And there is a lot of tension. And there's even tension on the supervisory side. You always want to make sure examiners are objective and independent.

And that's a struggle sometimes if they're at the institution a lot. But I think one of the things that I see, for example, that is really heartening is we have supervisory staff onsite that will be monitoring the institution and see something that they're doing. And now it'll trigger thoughts as to that might have implications in resolution.

I should talk to my ready staff (phonetic). And so we're addressing those issues up front rather than getting to the end and then I didn't realize this. So I think it's a really great question. There is a lot of tension. But I think having the discussions really works.

MR. MCGRAW: Yeah, we had -- actually, John and I sat through a briefing two weeks ago where one of the supervisory staff was on an examination. And there was some issues that were discovered that really created a lot of questions. This could really make a resolution really difficult.

And so we sat and we talked about that. So somebody who's an examiner by trade but was thinking about the implications that these issues were uncovered during an exam would have on a resolution situation. Yeah, Richard?

MEMBER HERRING: I was intrigued by

the cultural difference you noted that inspired the formation of this integrated group. And I think it does make a lot of sense. But I also noticed that internationally we really still have this strong separation between the supervisory colleges and the crisis management groups.

I'm wondering how much of an overlap in membership there actually is and whether other countries actually have the ability to join the two approaches as you do because you have both a supervisory responsibility and a resolution responsibility. My guess is Elke doesn't have such easy access to supervision, but I don't know. But it does seem logical that those two entities -- and there are all sorts of privacy concerns and disclosure of information that would have to be dealt with. But I'm curious about how broadly you think the model can be applied.

MR. CONNEELY: Well, I think the FDIC really is in a unique position in this regard. We have statutory supervisory in a backup role, authorities on the supervisory. And plus we insure, so we have responsibilities and authorities on the insurance and deposits.

We're also a resolution authority. So I don't think there's too many entities that have that combination of authorities. And it puts us in a unique position which I think we're trying to leverage.

MS. K™NIG: I think you spotted the right problem, and that's the problem to make sure that supervisor who holds onto his child doesn't hold on to the child far too long. And in Europe, we are trying to solve it in our institutional framework a bit similar to what you do. We are participating in discussion of the supervisor which for the banks in our realm, it is Frankfurt under the ECB.

And at the same time, we have them participating in our discussion. But I think it's a topic that you always need to keep just on your mind because it's a bit -- it's my problem and the White Knight is just around the corner to avoid that kind of debate. Now you're in a better position because you also have supervisory powers.

We have formally the chance to do onsite inspection of the deep dives. But we would always be a bit in a situation are we doubling up to what the supervisor does because we are not the supervisor. But in principle, it's the same idea that you have between putting this into one group to say we need a very constant dialogue also with a supervisor. And over the eight years, we have developed out of the discussion on why do you need to know. We have now full access to their information on the supervisory side.

MEMBER PETERSON: You mentioned that you have supervisors on site, but that's only a few people. Have you changed your expectations of the role of internal audit as well as the audit committee of the boards?

MR. MCGRAW: I would say, no, we haven't changed our expectation. I think the expectation is still the same. But we do have a small number of onsite given that we're backup supervisory. The OCC and the Federal Reserve numbers exponentially are higher than ours. And so we do work closely with them.

And we do look at audit and where audit is considered to be reliable is strong. We'll look at that as far as thinking about have issues been remediated at the firm. If audit is credible, then that'll go a long way with us to see what their findings are as they look at different issues that the firm has addressed.

MR. CONNEELY: I would just add -- I'm sorry. I would just add that it's not a shift or difference. But there is an extension now. Audits now focus on resolution issues, and we leverage off of that.

And so that's a good development in the firms and the banks is that they're auditing resolution issues. They're auditing their calculations and their capabilities so we can leverage off of that. And so it's an extension, but it is relatively new.

I too was thinking about the tension between the supervisors and the resolvers here, the potential tension. Now a lot of resolutions are triggered by liquidity runs, right? So then the supervisor has no choice, right?

But the key would be trying to get in before the run and the fire sale. That would be really a stabilizing intervention. So could you talk -- and the data coming in on what the actual capital of the institution is, is very lagged and incompletely and asset prices are changing very rapidly. Could you talk a little bit about what would trigger the resolution before the liquidity run?

MR. MCGRAW: Yeah, I would say again for us it's having those conversations. We bring resolution as a part of the process throughout. So if we're starting to even notice that a firm is starting to experience some stress well before you get to an actual liquidity event, we've got our resolution people on board.

Again, through that escalation

protocol process, we'll meet. And okay, there's more risk here. We're seeing some stress. We're going to move this firm down.

And then that triggers resolution readiness starts doing more to start preparing. So there's not a, well, there's an event now. We've got to prepare. All the preparation is going to be done up front prior to that event actually taking place.

MR. CONNEELY: One thing I will add to that is that one of the authorities we don't have is we don't charter institutions. So it would be the Fed or the OCC or the states. And they're the ones who would make the decision as to whether or not to pull the keys. But having people there, we're doing the monitoring so we're real time.

MR. FELTON: If I could jump in. It might also be worth mentioning that one of the -- the real benefits of the Title I review work over the last decade really has been improved internal governance mechanisms, quantitative triggers, the improvement. And this is also from the supervisory side, internal modeling, capital stress testing, liquidity stress testing so that even if the regulatory capital numbers don't come to us for four weeks that the firms are expected to have as close to a real time view of that as possible and that they have internal governance mechanisms to start engaging in actions as necessary.

MEMBER KOHN: And they share that view with you.

MR. FELTON: Yes.

MEMBER TAHYAR: In the GSIB SPOEs, right, there's our language is liquidity execution need which is calculated daily. It's shared with the supervisors. It's never been tested, so we can't say it's perfect or that it would work in real life.

But it's massively better and different from what we had in 2008. So I think that if a GSIB were to go into resolution, itself it would be pushed into the bankruptcy far before the chartering authority pulls the plug. And our line is what is going to tell you to do that.

MEMBER O'CONNOR: Just one other question to ask. To what extent or how are you working or integrating the evolution of markets, particularly the Treasury markets into your analysis given that the liquidation of collateral is so foundational to both recovery and resolution for banks, nonbanks, CCP in every structure out there?

MR. CONNEELY: I'll start. We recognize that and we have started looking at that. And I don't know if you have anything you want to add to that.

But it is an area that we don't naturally -- as supervisors, we don't naturally have insights. We're not the Federal Reserve here. But it is an area where we've seen time and again issues occur and issues that affect our institution. So we are looking now at building up our capabilities in those areas.

MEMBER O'CONNOR: So just as part of

the advisory board, I would continue to encourage you to look at that interoperability, right? Because we've got shifting credential rules that had implications on markets, on Treasury particularly. And we have that reliance. And this is a circle. So I think those are very important things, and I'm glad you're looking at them.

MR. MCGRAW: Yeah, Andy and I have had several discussions over the last several weeks about building that out more within the systemic risk range. Hi, Tim.

MEMBER CLARK: Hi, just a quick question. I think the coordination is a great idea. I'm glad to hear it. I hope the interagency coordination was still functioning as well as it was when I was at the Federal Reserve.

Focusing on the supervision side, the goal here is really for these firms to be prepared for resolution and frankly prepared for recovery action so they never get to resolution. Plans are great. The finding of credibility of a plan is a challenging issue.

Credibility frankly of a plan for one of these firms to be resolved in bankruptcy, it would be a huge challenge. So on the supervisory side, you have an opportunity to really push in areas that can help to make the firms better prepared and more thoughtful internally hopefully. But I wonder. I guess my -- there's a question coming here eventually.

(Laughter.)

MEMBER CLARK: There's been a lot of discussion about whether the agencies are creating rules through guidance. This has been very prominently raised by the bank policy institute. And it's interest because, of course, guidance has been somewhat undermined a little bit by statements by the agencies over the past few years.

I'm wondering if you think that the way that everything is set up right now is the most effective way for you to achieve getting these firms to be better prepared or if you think that possibly strengthening some of this guidance into a more rules-based approach would eliminate some confusion and take away some of the criticism that the agencies have faced for making up rules without actually having a rule which frankly I think is unfair. But it's a long question. Was that clear enough? I can repeat, but it was long.

MR. CONNEELY: No, I think it's clear enough. We're the practitioners. We implement and try to implement the guidance, the rules, what have you. I leave it really to policymakers and others to determine whether those should be rules -- guidance should be rules or what have you. But yeah, it's a good question.

MR. MCGRAW: We do have a lot of authority in Title I, for instance. And I think there are ways to -- again, thinking about the supervisory side and how that impacts Title I capabilities, et cetera. There's a lot of authority there that can be used and to push firms to get issues fixed that have direct implications on resolution readiness.

MEMBER CLARK: Part of my question was, has any of that ability to influence through that manner been undermined by the talk of guidance shouldn't be taken too strongly. I'm just trying to get a sense of how the dynamic has changed given all the discussion about making rules through guidance again I think has been unfairly aimed at you.

MR. MCGRAW: I would --

MEMBER O'CONNOR: I'd like to hop in here. I think broadly speaking when guidance is given, forget about what the guidance is. Clearly, financial institutions need to take that extremely seriously because of the ultimate assessment of whether or not your plan is credible. And then I think there were discussions broadly around what would the implications of certain types of guidance be. So I think the reality is there can be guidance and, two, yes, it's taken extremely seriously.

ACTING CHAIRMAN GRUENBERG: And if I

could just add when we implemented Title I and Dodd-Frank, we started with rulemaking. That's detailed and really lays out the framework for implementing the Title I authorities for resolution plans. And we elaborated on the rule as you well know through guidance documents to provide greater detail to the institutions for implementing their requirements established under the rule. So I think it's been actually a pretty functional process.

DIRECTOR HSU: Questions for the committee. I think part of what the structure of CISR helps to do is address these twin problems. One is that without that integration, I think resolution risks becoming a paper exercise the way it's kind of set up.

And part of that is the second problem which it's very infrequent, right? So I mean, knock on wood. That's the intent. But part of that means that memories are short and people forget.

I think on a lot of these resolution

issues coming out of the '08 crisis, everyone was moving in the same direction because it was so present. It was omnipresent as an issue, both on the regulatory side and on the bank side. And as we get further and further from that, we've got folks having lived those things, part of the challenge is not having it just live as an ivory tower exercise over here and then you've got kind of day-to-day supervision risk management over here.

And I think part of that integration is key. I'd be curious to hear from others. Like, what else needs to be done to keep that front and center? Because I think this gets back to an earlier question about boards and audit committees.

That's kind of the daily muscle with an organization. And I think it's very easy to just say, well, that was a long time ago. We've figured this out. It's all good. We can move on from here.

I think that's going to be a perineal

challenge, especially as we move forward and there's new risks that come up. And I think you guys were talking about that. I don't know if folks have thoughts on that.

MEMBER ERVIN: Yeah, I'd share that view. It's one of the problems you have a peacetime Army that doesn't get to fight. And unfortunately when combat comes, you need lots of troops. You need to get them on board yesterday.

And that strikes me as one of the fundamental problems that you have in an agency like this. How do you keep some of those memories alive? I teach some classes to kids who think 2008 was a million years ago, right?

And there's a generation of people who lived it, and that generation is slowly moving on. So I do wonder if there are training exercises, ways you can kind of throw in. There have been some war games.

I remember actually Jay Powell ran one of those things a long time ago which was quite useful. They had a former FDIC chairman pretending to be an FDIC chairman on the panel. But throwing in curve balls and throwing in multiple actions into the market and trying to at least get people to think about that as more of a real time exercise.

I think different types of training might be one way that you could preserve that a little longer. It's a tough problem. But I do think your point is very well taken because these things probably don't come in ones and twos when they come. You look at some of the FDIC history, there's some pretty big waves. So I do wonder if there are ways you can use some of those tools to help with that.

MEMBER O'CONNOR: I would encourage also the cycle. Keeping the cycle reasonably short, two years, three years for the institutions because systems and approach can atrophy otherwise. So I think that's important.

The second important point back to what Wilson was just saying is also on the crisis management groups, really doing play book exercises because again within five to ten years, everybody turns over. So many of us in this room who lived through all of it will not be sitting around those tables. So I think that's equally important because those two things need to come together.

ACTING CHAIRMAN GRUENBERG: If I can just add, and it's an important question on the standing Army issue. How do we mobilize in the event of a stress environment? And we perhaps should've had the table -- in addition to these folks who spend their time on the supervision of the largest institution and resolution planning for the largest institution, we have an additional division dedicated to resolving banks on the smaller end of the spectrum but with very significant operational capabilities and frankly large human resources to draw up which also collaborate closely with these complex institution groups.

So we actually can bring a lot of resources to the table in the event of a stress scenario. And a large part of the planning of those groups are if we had to mobilize additional resources. You actually have standing contracts with third parties if we need to as well as capabilities to call back retired annuitants. I mean, there are in place a whole set of plans that we --

PARTICIPANT: Reservists.

ACTING CHAIRMAN GRUENBERG: Yeah, to draw upon. And particularly even now, for example, where we may be facing -- we are facing a change in the economic environment and uncertain outlook of what the next 6, 12, 18, 24 months may present. And that triggers a lot of thinking on both the supervisory and on the resolution in terms of additional human resource needs and how we might address them as events unfold.

MS. K™NIG: Perhaps to add and not to get so militant like Army. But we are firefighters.

(Laughter.)

MS. K™NIG: We hope there's no fire. But we need to be trained for all kind of fire and not just to believe it's the old chimney that will burn and this is where you know the answer. But what I find incredibly important I think the way you're setting it up, it addresses this is the cooperation then also between the various institutions.

Now I come with a European mindset. We have 21 national authorities. So you never know which country will be the one you have to deal with. But I find it incredibly important for any cross border institution that we also train together, have deep dives, have a kind of tabletop so that we all speak the same language and that we all know what we want to do and how would we work together, be it a European institution with a U.S. arm to it or be it a U.S. institution with in our case simply be across European institution. So testing and fire drills are probably the only way I would think of to do so.

MEMBER COHN: You're probably going to say the same thing. So look, we're all creatures of our past. So when we go through all this resolution, even though we may be forgetting '08, it still heavily influences everything that we do, that we think.

I think one of the things that we should be really careful about is the next crisis won't be '08. I don't know a lot. I just know that. I know that for sure. I know that for sure.

So if I was thinking -- if I was sitting in your chair, I would think what is the seismic or systemic crisis that's not '08? What happens if we get a major cyber event? What happens if we get a major cloud event?

We could just go through these. And how do we deal with those events. And '08, whether we like it or not, there was a sign, there was a windup, there was a pitch, there was a swing, there was a ball flying out. There were a lot of balls that went out of the stadium. We sat there and watched them.

The next event, there might not be a sign, a windup, a pitch, and a ball. It just might happen. And so in many of these things, I think we've got to accelerate our thinking because we live in a highly accelerated world. We also live in binary outcome events. And the event mostly likely will affect multiple institutions simultaneously.

MEMBER CLAYTON: Yeah, look, I agree with what Gary said. And a question related to that, I think March 2020, it was sort of all hands on deck for a little bit with a little bit of -- but not the same as '08. I'm curious. When was the last time it was sort of all hands on deck for a resolution even as an exercise? And I think that's -- if it's been a long time, it's a good reason to give it a try.

MR. CONNEELY: Well, I think 2020 was all hands on deck. I think the market events that we've had was all hands on deck. The geopolitical events we've had all hands on deck.

Some of the instances that we're going to share with you today any one of these -- to your point before, any one of these could cause a crisis amongst our banks. We need to be ready all the time, and we really don't know when it's going to come. And it could come very fast.

So we do maintain a heightened state of readiness. We do exercises both internally and with other agencies and globally. We have protocols and committees set up to constantly work through some of these things.

We can't predict it, and we try to build our resolution tools so that they're functional and they'll work in any sort of environment. But we really don't know what's going to happen. But we try to maintain a heightened state of readiness.

MEMBER CLAYTON: And just to follow up on what Gary was saying, unfortunate experiences, every time we go through one of those, you're like there's something I wished that I had. And it would be interesting to get updates on what those things you identify that we didn't have this going in but we could use it the next time.

MEMBER O'CONNOR: Yeah, just to amplify those comments as well, I think you have two things here to add. Big picture, how do we horizon scan in a more effective way? And how do we contemplate an economy that is substantially more open, right?

You don't have the banking industry writ large as a choke point for the bulk of financial services delivery anymore. You've got open technology architecture. You've got open nonbanks. You mentioned that a little bit. So as you think about continuing to shore up this section which is super important, it's sort of like a balloon.

And the answer may or may not be regulate more, expand powers. But how do you think about -- how can we think about under the powers that you all have in collaboration with the other agencies to identify and address these types of risks as they emerge? Because in the end, people are going to care about was the economy impacted by financial instability regardless of where it came from.

MEMBER COHEN: John, you had mentioned right in your introductory remarks that the last time we met, we did not have -- you did not have the data which you needed for nonbank financial institutions. This is what the chairman generally mentioned about nonbank financial institutions. In the beginning, I gather you don't -- you still don't have -- I got to believe that this creates a problem not only for the -- I mean, you have no ability with the nonbanks. I would think it adversely affects your ability to really supervise and plan for the regulated sector. So if all of that is still correct and to go to what Jay said, we've got a gaping hole and the nonbank sector grows.

Now I want to take a radical approach, suggestion, and go back to something the director mentioned again in his opening remarks and that is FSOC. There are huge problems with designated and regulating nonbank institutions under FSOC. Why could not FSOC designate just for the purpose of providing data, requiring data to come to you to give you a better overview of what's going on?

ACTING CHAIRMAN GRUENBERG: I think these guys are going to find that question over their head.

(Laughter.)

ACTING CHAIRMAN GRUENBERG: But I think you raise an important question, Rodgin. And I think this is a subject obviously I think all three of us are concerned with as members of the FSOC. I think it's been a focus of attention if I may say for the Secretary as well. And it's a subject we're hoping to address.

DIRECTOR CHOPRA: So of course, the tools to get firm specific data to the extent there is a -- I don't think this will be that helpful but some state regulators that have some insight. But there's also the Office of Financial Research which has certain authorities to compel and collect data that has been used in a fairly limited fashion.

But it's also important to underscore the legal mechanics of using -- of invoking Title II. For a nonbank, it requires, I believe, super majorities of the Fed Board, the FDIC Board, and sometimes maybe even the SEC has to be involved, consent of the Treasury Secretary, maybe even consultation with the President and with no real insight as to what is happening other than market signals. And to be able to go in again without a supervisory relationship, without a plan. And yeah, tough.

But I don't know what we've -- what Jim, John, and others, if you want to share the thinking you have put into that scenario of how to navigate something like that. Obviously, it's like what Gary said. You don't even know. What are you even going into?

MR. CONNEELY: Yeah, it's a difficult question. I mean, we do try -- it's difficult. Honestly, it's so vast, both the authorities.

They're very broad authorities, and we don't know where the boundary is fully drawn yet.

I mean, there is some parameters that companies would have to meet. But we're in a dynamic environment. And then as far as what the decisions are going to be made at the time, there's going to be several parties involved and they're always going to have their own perspective.

And we'll have to deal with those facts and circumstances at that time. It's hard to plan for that. We do hold conversations, though, with all the key turners to make sure everybody understands their roles and talk about issues. But it's difficult.

DIRECTOR HSU: I want to maybe try to tie together Gary, Jay, and Sandie's comment because I do believe that this challenge of how to prep for the next and not fight last year's war, right? It's kind of a perpetual challenge. The exercises that we're talking about earlier are really valuable. They're extremely time intensive.

And you have to pick wisely. And I think this is one of the challenges is, like, where do you drill? And if you pick that spot, then if you miss, then you expended a huge amount of resources.

So I think that does argue for something a bit more modular, smaller, faster, more nimble. What exactly that is, I think we really need to put some thought into how to do that because I think that is a newer -- because I think the environment requires it. Because change is happening much more quickly and things are not contained within the four walls of the bank anymore.

And so that does require kind of a bit more creative thinking on that front. It would be interesting to know what other industries do, kind of what's best practice out there. That's something that, I think, kind of the collective knowledge of folks at this table and your friends have probably some insight into. So that may be something to kind of think about and pursue in the future. Thanks.

ACTING CHAIRMAN GRUENBERG: May I just observe, this is really a pretty engaged group here. And I'm looking at the clock and our agenda this morning. And I'll maybe perhaps move to our second agenda item.

And I think all of these issues continue into the next. So it's not as if we're leaving them behind. But I actually think these next topics will engender further conversation around these issues. John, if that's reasonable.

MR. CONNEELY: No, I think you're absolutely right. We're actually naturally leading into the next panel. Thank you. And our next panel which is going to be the resolution planning update as we noted, Title II and public transparency and large bank resolution planning. And we'll have Deputy Director for Resolution Readiness Ryan Tetrick, advisors Betsy Falloon and Susan Baker, and our legal counsel Pen Starke.

MS. FALLOON: Thank you and good morning. I'm Betsy Falloon. I'm a senior advisory in the resolution readiness branch. And I'm here to introduce our Title II topic for today.

And chairman and John have mention that what we're interested in here is to talk about transparency and ways that we can tell the story of the way we are planning and the way we intend to approach a Title II resolution in a way that enhances everybody's understanding of it and improves confidence in the process and the outcome. At this point, there's a pretty broad awareness of the single point of entry strategy. I think that people are aware of that approach to resolution which is the one that we think is the most effective.

And a lot of steps have been taken to make that approach more actionable, more available in a wider range of scenarios, both in Title II planning area but in Title I as well. The firms have taken steps and the agencies as well to improve the firm's structures or capabilities. And the single point of entry strategy is now a credible option in a much wider range of scenarios.

The planning work in Title I has certainly had a lot of benefits and our Title II readiness as well. And sort of the talk about the firehouse or the standing Army, that routine of the resolution planning also helps us because there's always new information and new plans. And we are building upon our planning as the firms build upon their planning.

So over the course of my career, I have seen where resolution planning has become a truly full time year round job which is way different than in the early years where we came in and out in good time to do deals and a bad time to do resolution. But we recognize that this is hard. And comments have been made about how it's hard to know exactly what to be ready for.

And we certainly know that being ready

for the last crisis is not the answer. Although certainly also we need to have learned from the last crisis and remember those lessons and keep that muscle memory but at the same time not be trapped by the expectations of the past. As I mentioned, we use the Title I plans as a foundation for our resolution analysis in Title II.

And in Title I reviews, we are now using capabilities testing more so that as part of our Title I review. So to validate the capabilities that the firms have described in their plans and the capabilities that we rely on in Title II for our readiness. Arlen (phonetic) was mentioned, and that's certainly a capability that we think about a lot in Title II readiness as well as in understanding the risks associated with the Title I plans.

We have a systemic resolution framework that we have built out which is sort of our road map for how we think about Title II execution. And we've been working -- at this point, we're building in details. We're building in templates.

We're trying to make this framework an actionable set of steps. And an important part of that is internal tabletops and exercises. We try to do a lot of that, both the high investment, high yield ones where if we get it right, it's really good. And we've had a few of those.

And also, we try to look for opportunities where we have low cost exercises. We call them Pop Exes, but just a quick, not a lot of buildup, how would you do it if this happened. Take this firm. Take this scenario. Send some staff and go.

And those are ways that we can -- I don't want to say build muscle memory because it's not quite true. But create the teams, create the expectation. Keep the knowledge fresh, and also identify where we have gaps and where we need to do additional work.

Certainly coordination among all the

financial regulatory agencies is critical to our readiness. And I think John mentioned the ongoing work that we do with key turning authorities which is really important. And we also coordinate on a staff level with staff at Treasury to make sure that the liquidation fund which is funded ex post and is a different approach than what we use with the deposit insurance fund that we have a staff level understanding of what it takes to make sure that we're ready to move that money timely and that everybody knows what their job is to accomplish that.

And of course, there's been a lot of talk about our cross border engagement. And in CMGs and outside of CMGs, we have a lot of engagement with supervisory and resolution authorities around the world to make sure that we have as much as possible shared understanding of the steps that we might take, the steps that they might take. And that we talk about the work that we've done to keep those issues fresh and to keep those relationships fresh.

And all of this really supports readiness and keeps us busy while we're in the firehouse. Next slide, please. So the topic here is transparency. And we are very mindful that confidence is critical to the success of a resolution in any case and in every case but particularly in this case where we would be exercising authorities for the first time.

And the key to confidence always is setting expectations. Do stakeholders understand the process? And is it being executed consistent with those expectations?

So we have taken steps to build awareness and understanding and are sort of looking for ways to continue to do so. So for instance, we've been very transparent about our Title I resolution planning work. The guidance is published. Q&As are published.

Public portions of the plans are made available to the public on the agency's websites. Our feedback letters are open to the public and are also posted on websites. So it's an open process.

And I think that there's a lot of information available there. Certainly I've mentioned that we work with other regulators and regulatory authorities to have a shared understanding with those stakeholders. And in 2013, we published a notice in the Federal Register about the Single Point of Entry approach to resolution and to make that strategy that we had developed available so the public and other stakeholders would understand and be aware of that approach to resolution.

We continue to talk about Title II resolution. There's been speeches about it. We talk about it in a lot of different venues, some of them are in small group venues and some like this one are open to the public and are a way for us to tell our story. But what we want to do and what we want to ask you about is what do we need to do to better set expectations to power our communications and improve confidence when the time comes. And with that, I'll turn it over to my colleague, Susan Baker.

MS. BAKER: Hi. As Betsy conveyed, we've done a lot about transparency in terms of resolution planning. It's all out there on the website. What we want to think about and what we're starting to work on now is how to improve transparency about our execution plans for Title II resolution.

We've been working on these for ten years now. And we should probably be starting to say more things publicly. So what we want to think about today is what should we be transparent about now that would help improve confidence in the event that we're called to use our Title II authority?

So we've been thinking about this across many dimensions. First, we look at who we need to be transparent for. And we have a large number, a list on this slide that you can see.

We've done a lot of work with policymakers and regulators around the world as has been said and a lot of engagement with certain parts of the firm. So the sides on the right, we've probably done more on. But what do we need to be thinking about for the stakeholders on the general public, customers, counter-parties, other people like that?

We think about what message do these stakeholders need to hear. And it might not all be the same. And then we think about when we need to be transparent.

And I know that there's going to be a temptation for us to say -- for people to say FDIC should just lay it all out there. Say what you're going to do every step along the way. And that pre-commitment will help improve confidence.

But we also need to be mindful of the need for FDIC to have operational flexibility to adjust to the specific facts and circumstances on the ground. Next slide, please. So the is slide is some topics that we're considering, the what of what we need to be more transparent about. And so what we would like to hear from you is which of these topics or others that might not be on here, thinking about contracting authority which I took off the slide and now maybe I shouldn't have.

(Laughter.)

MS. BAKER: What are the things that would be helpful to get out in the public domain to improve confidence now? So some of the things we've heard about obviously are what are the key decisions that the FDIC has to make, when would you decide the framework? Is Title I bankruptcy going to work or do we need to turn keys for Title II which basically hinges on the need for liquidity through the OLF I think?

How do we decide the resolution strategy? Does the firm have enough capital to make an SPOE work? Or do we need to be thinking about an NPOE?

Do we need to be more transparent about how we coordinate cross border? How it would differ if we're a home or a host, for example? We get questions about planning for the bridge as well.

Who's going to run this bridge? What assets and liabilities will go into it? And how will the FDIC oversee what's happening at the bridge and maintain that for public confidence perspective as well?

We're thinking about creditors. How do you communicate with claimants, including about their claims determination? How will the losses be allocated on the Dodd-Frank hierarchy which is different than under FDI Act and under bankruptcy?

And then how with the claimants be compensated? How does securities for claims process work? We mentioned that in the 2013 thing that Betsy mentioned earlier.

We're also wondering if we need to be more transparent about some of the accountability mechanisms that we have as well for the general public audience. We are required to remove culpable management. How would we go about doing that?

Do we need to reemphasize that in the Dodd-Frank hierarchy, that compensation claims are subordinated to general creditors and that prior compensation could even be clawed back if needed. And then finally, there's the funding mechanism. What part of that would be most helpful to provide confidence.

I do think that the OLF in using it as the big gift -- it's not a gift, but the big tool that we need in Title II to help provide confidence. But what do people need to know to really get that? How important is it to explain the rules and the mechanics for the OLF, how money will get from point A to point B.

How would we use targeted guarantees to allay concerns about excess cash use? There's a lot of questions here. And so there are a lot of things we've been thinking about.

And what we want to hear from you today is what you think the priorities would be in order to go about setting expectations appropriately in public about how we would execute Title II so that if an when we do have to have that announcement on Friday -- ideally, Friday night that people are in a position to receive it, understand it, and say, yeah, that works. And we can see how this will happen. Of course, there will be doubters. But there's a lot of things going on. So with that.

MEMBER HERRING: First of all, I'd like to praise the FDIC for its unrelenting pressure to have more disclosure under the actual public reports. I think they have been very helpful. Second, I guess I am a bit pessimistic about your ability to communicate with the people who really need to know in terms of a crisis. And this is partly from my experience of teaching this stuff.

(Laughter.)

MEMBER HERRING: There was a lot of interest just after the crisis. It's dwindled over time. And so people are sort of less and less interested in getting into the nitty gritty and some of the really interesting developments.

So I would think your strategy ought to be to disclose as much as possible to people who professionally need to know about it. And that would certainly including the ratings agencies, the people within the banks who are responsible for these judgments. And simply publicly available, a place where people can go if they need to know more because we're dealing with a society where people are getting their information in tweets.

There's just no patience, I think, for going through the elaborate and careful planning that has gone on. It should be there. It should be accessible when people need to know. But I don't think you have much hope of reaching a public that doesn't have a professional need to know.

MEMBER COHN: I completely agree with that. I almost think you'd scare the public if you put this out. Like, why are they telling me this? Should I be concerned about my bank?

Like, my insurance company doesn't

tell me what they're doing with my assets if they just assume they're going to pay my claim, right? I think you've got to think of the unintended consequences of taking a public that has more full faith and confidence in the banking system than maybe people in this room do that we want them to have full faith and confidence in the banking system. They know the FDIC insurance is there. They know it works.

They put their money in. They're going to get their money out. So there's a select crowd of people that are in the institutional side. And if they won't understand this, they're going to find a way to understand this.

There's a bunch of law firms represented in this room. There's a bunch of people that'll change them by the hour a lot of money to explain this all to them. And I don't have a problem with that, and they all have huge staffs. But I would be careful about the unintended consequences starting to blast too much of this out in the general public.

MEMBER TAHYAR: So I'd like to take a slightly different view that may be a middle ground in the center. First of all, I think Susan and Betsy, what you've done and the thoughtfulness here is extraordinary. And I want to give you respect for it.

I do think there's more that could be put out in the public, perhaps not just on Title II but also in Title I in a way that isn't scary to folks. I mean, Gary, there's a timing question, right? We're at a delicate moment now.

So if it goes out tomorrow, it might have a different impact than if Susan and Betsy do their work and it goes out as we're moving out of the recession. But I'm very big on transparency. I think transparency leads to accountability.

The FDIC has to have flexibility. So there are some ways that you could get out some basics which say, we could do this, we could do that. We will be holding these folks accountable. We have these powers. We have these authorities.

Without putting too much out there, I get that we live in a tweet world. But you know that 1994 book that the FDIC did on this, I mean, that's a bible, right? And so folks who want to know about it want to know about it.

One final thing is I think there's an additional group of stakeholders that exist today that need to know more about resolution planning that didn't exist when we started on this journey and that is the kind of fintech nonbank lenders, money transmitters, digital assets, crypto exchanges, whatever we want to call them. I know you've listed domestic authorities. And I think there are states that are starting to think, should we have a resolution plan?

And there's so much learning here that could be of benefit to those who are thinking about different kinds of resolution plans. And they would be very difficult if you could put a little bit out more in public. So I'd go for more, maybe not the whole hog.

MS. K™NIG: Perhaps to build on those comments, I can share we were -- when I go to Parliament, the first question is, when will you become more transparent? The second question is, when are you giving us more information? And then when we published in summer, or first assessment of resolvability, I could count on Germany's paper at least commenting that we published something.

Then our gossip magazine, political had a short article and that's it. When I went to Parliament the next time, they said, when will you be more transparent? When I refer to the is, I knew no one had read it.

(Laughter.)

MS. K™NIG: But I think the simple argument is -- and I would I full heartedly build on your comment -- you need to probably have on your website and I know you have already a lot on this. How does Title II work? What can you expect from the institutions to do in case of, a bit stylized.

And this can go out on a normal sunny day. You need to be mindful that it doesn't go out and everyone is quite sad. Why are they doing it now? But I think a number of the other topics are probably topics for what we would call it guidance paper where you give more detail to those that have either an academic or an institutional desire to know.

But they are not really top of priority for the public. Now the one difference between us I have always envied for that is that you have the summaries of Title I plans. We are not talking about any individual banks, so you will find from us a comment on GSIBs. On average, everything is fine. You will find a comment on midsize and the like. But you will never find any detailed bank specific comment, a topic that all Parliament is talking about.

MEMBER O'CONNOR: So just to sort of again looping these three together. From my perspective I think when you're going to make --

I believe in transparency. But it has to have a meaning.

So if the people that are getting the transparency need to be able to do something with it. So for example, when we have a terrorist alert and we give it a color but we don't know where it is, how we respond, that's transparent but not particularly productive except that we should worry. So I think here we've got to do this sort of same sort of thinking.

How and what should be used by the general public. And that's sort of minimal and sort of basic framework. And two, what transparency can you provide that will lend stability in a negative outcome?

And that's more about not publishing claimant communication. That's going to be more about you're going to come out and say we've got this. We've got a strategy for this. We are confident we can work through it.

So that's sort of I think the way that you should be thinking about the communication.

And with regard to accountability, yes, that's at some point. That's sort of a stage two.

I think you definitely need to do it. But that's not your first order communication. You're first order communication is we've changed managements, right? So those would be sort of the framework that I would offer up to think about which I think you sort of have here.

MEMBER ERVIN: I'd like to go back to some of Dick's earlier comments. I do think it is hard to get a lot of demand for transparency right now in the is sort of period of peacetime. But that is going to flip, and it's going to flip probably even faster than we saw in 2008 where the need for communications really quickly in the social media world to avoid disinformation and have some holding patterns for things like I remember in the early days of bailing people saying they're coming for my deposits, right?

So just holding communications that you can pull out that are helpful to deal with disinformation, some very simple things, and how quickly you'll be able to deal with different constituencies. For example, liabilities are further up and closer to harm's way. When are you going to be able to give them some comfort, if any?

How do you deal with foreign operations? How do you communicate to some of those different groups? I think ex ante preparation for the speed of scaling up and the ability to get information out to avoid rumors taking over the narrative strikes me as probably the place that feels like it's got the most benefit in a world where I think you've done a pretty good job of getting out the basics of Title II and some of the basic resources that are available now.

MEMBER LA SALLA: Can I just make a general comment which will be totally unhelpful and unproductive because I don't know the answer to it. But it never stopped me from saying anything like that before, so I'll do it again. Transparence is only helpful and effective if it's accurate.

And that sounds obvious. But in my experience with resolution issues, and in this world in interoperability between institutions, it seems to me more times than not the regulators are sort of the quarterback in this. And they're getting bilateral information. But the normal network of institutions that really should be talking to each other to help aren't doing it.

And so information becomes disinformation because everybody is waiting for each other to clarify. So my point is to have accurate transparency, it needs to be underpinned by a foundation of a solid normal network within the industry among the institutions who are involved in this. And that's not easy. But I think it's something that we need to really think about and work on because if we don't it's just going to spin.

MEMBER CLAYTON: Can I follow up on that? I think -- look, I think this is an incredibly important point. And any statement that's made whether it's made by a regulatory or an institution is going to be tested by the market.

And we have to understand that. And I think that just putting the two points together, what you want to have out there today is something that when you make a statement in a time of stress, it provides that underpinning for the statement. And I think that's the way to think about the body of work that you have out there, and it's kind of a dynamic relationship for when you have to make a stabilizing statement.

MEMBER KOHN: I wondered whether there are some market tests of whether you're being heard. And I think about TLAC. So TLAC should spread, should respond to good and bad news about the institutions. And it's really important. I mean, it's a little bit conflicted, right? I mean, it's important that people understand they can be bailed in.

But you don't want a huge run on the

institution. But they're going to be, and it could be an early warning signal to the FDIC and the primary regulators when these things happen. And there may be some other prices -- this is similar to what Jay was saying -- in the market that you can tell whether people understand who's going to be protected, who isn't going to be protected. It would be, I think, an interesting study to look at the evolution of market prices in the situation like March of 2020, for example, and see whether people understood what might happen.

DIRECTOR HSU: I might go further than that, Don, because I think that you look at the evolution. I think we have to sit down and talk to long-term debt investors and make sure that they as a stakeholder group fully understand bank debt today is not what it was before. It is not principle protected by design. And I think that expectation, I like how you started off.

It's all about expectation setting. And I think that is absolutely critical. If that doesn't hold, this whole thing doesn't hold. So I think it's one area to focus on.

I do want to go back to something Jay said about stabilizing statements. In my experience, they're not stabilizing. If you have to make a stabilizing statement, you're in real trouble. And I think that part of that means there's a lot of pre-work that needs to be done such that those statements aren't seen as a reach.

Because if they're seen as a reach, the market sniffs that out in two seconds and actually has the opposite impact. And this is one of the big challenges. Like, what can be done ahead of time so that it's all going as planned, hands off the wheel, this is part of what we've been prepared for? Because that's what builds confidence.

MEMBER CLAYTON: You just said very well what I was trying to say.

(Laughter.)

MEMBER PETERSON: So I think the most

stabilizing comments have not been coming from the FDIC. They've been coming after the CCAR tests. And so there's been a consistent approach now for over ten years of pronouncements coming out about the banks, about how much capital they're able to return, how much stock they can buy back, what kind of dividends they can pay.

And that consistency, the market understands that. Even the common public will understand that. They know how to read those headlines.

I think what we've talked about here with the FDIC's role of having this available for institutions, have it available somewhere. The professional markets understand it. But I think right now the more stabilizing factor is that we've had ten-plus years of reports on stress testing, on capital levels, on dividend levels, et cetera.

And maybe we should think more about is there a way to make that more transparent or eliminate some of the jargon, et cetera. But what you're doing I think is excellent work. But maybe it should be more for professional investors and available to anybody.

MEMBER ERVIN: Just a quick comment back to Mike and Mike's comments about TLAC spreads and Don's as well. I still kick myself for not buying some during the COVID crisis. They went --

(Laughter.)

MEMBER ERVIN: I feel stupid about that. There have been some events in Europe over the last decade. And TLAC and CoCo spreads have spiked out and come back in on idiosyncratic stuff. So I think the market has generally been behaving as we would hope it to behave. Some of the academic studies I've seen, I know Darryl Duffy (phonetic) and a few people did a big study on some of the too big to fail premium. And it seems to be working okay.

Again, we haven't really run the thing through a proper test. I hope we don't have to in the near future. But at least all the ex ante signals about credit market spreads and whether it's systemic or idiosyncratic seem to be sending decent signals from what I can tell.

MEMBER HERRING: Following up on that very quickly. In the very early days of the committee, we used to measure sort of how well we were doing with whether the kind of debt we were looking at, at the bank or at the holding company, differed. And it was really a couple of years before the markets got the message that there really is a different credit risk here, that there are different priorities in play. So I very much would support Wilson's view, and that's a healthy thing. Somebody understands the rules which is good.

MR. CONNEELY: Well, this is a fantastic discussion, and thank you for all your input. And I think it confirms a lot of what we're thinking and it gave us a lot of new things to think about. We're running well behind on the agenda here which is not a bad thing. But I'd like to turn it over to Ryan Tetrick to talk about the resolution of non-GSIB large banks.

MR. TETRICK: Thanks, John. And part of the lesson of resolution planning needs to be prepare to execute on a compressed timeframe. See how this goes.

(Laughter.)

MR. TETRICK: So if we can turn to -- so we're on slide 14. So I should just start by acknowledging that this is the first time that we're discussing a large bank resolution in the SRAC and explain why we think it's the right time to do so. The policy response to the great financial crisis understandably focused on the largest and most systemic institutions.

At the same time, we at the FDIC have taken a number of meaningful steps to improve large bank resolvability and have long been attentive to the significant challenges that are posed by what are sometimes referred to as regional banks or DSIBs. But I'll simply call them large banks for this discussion. While compared to GSIBs, the failure of a large bank might be relatively less threatening to financial stability.

It still may be highly costly and result in significant disruption to local communities and potentially to the wider financial system, especially if it occurs in the context of a wider economic downturn. Our goal for this presentation is really simply just to introduce some of the challenges that we see with resolving these institutions and discuss some of the strategic options that might be available to us. During the global financial crisis, the FDIC handled the failure of the largest IDIs with creative and dynamic responses.

But the options that were available to us where limited and undesirable, a costly conservatorship in the case of IndyMac and the sale of Washington Mutual to a GSIB which was really only possible because it had a large preexisting stock of long-term debt to absorb losses and because it had already been marketing itself in the route to its failure. And so

JPMorgan had conducted significant due diligence by the time the institution failed. So it's fair to say that the challenges and tricky issues here are underexplored publicly and not fully resolved.

I promise we won't resolve them in this discussion. We'll just get started here. So really on slide 14, just a quick flyover of the FDI authority under which these institutions would be resolved.

The FDIA is the only regime available for resolving insured depository institutions. And importantly the depositor class is senior to unsecured creditors. And the uninsured depositors would share losses pari-passu with the deposit insurance fund which covers insured depositors. Every resolution must pass the least-cost test which means that the FDIC must execute the resolution that is least costly or a resolution that is least costly to the deposit insurance fund.

So that really comes into play only

when there are losses into the depositor class and therefore costs to the DIF in paying insured depositors. We have bridge authority which would work a lot like the type of bridge authority that we've talked about in Title II except that furniture depository institution, it's a new deposit taking entity charted by the OCC rather than a company formed by the FDIC. And it's well understood that the deposit insurance fund is available to fund the cost of the resolution in terms of the administrative expenses during the course of the resolution, the payment of insurance.

But really importantly for the resolution of large banks which will almost certainly fail due to liquidity. The DIF is a source of temporary liquidity as well. It's large, pre-funded, but also backstopped by significant borrowing authority ultimately by U.S. Treasury.

And the scale of the liquidity that we have in the DIF is actually in some ways greater than relative to the institutions that would be resolved or the liquidation that we're entitled to. So there's significant liquidity that we can use to facilitate one of these resolutions. So moving to slide 15.

Just quickly which institutions do we have in mind here? So generally in this discussion, we're talking about IDIs with over 100 billion dollars in assets that are not subsidiaries of U.S. GSIBs. But from a resolution strategy perspective, there's nothing magic that happens at that 100 billion dollar line.

There's nothing magic that happens at the 250 billion dollar line. The issues are really similar. They just become more pronounced as the institutions get larger.

Also, I think we find that large banks tend to be generalized as having a very simple structure. A holding company with 95 percent of all assets and activity in the IDI subsidiary conducting traditional banking activity. And part of the objective of this slide is just to break down that mental model just a little bit.

That holds for many institutions. But there's a little bit more complexity here than might first be apparent. Some of these institutions, they obviously have more diversified businesses than smaller banks.

And some of them even have Title I designated critical operations. In the first couple rows here, you're focusing on the impact of size on strategy. And again, there's not much difference between over 250 and under 250.

It's really a matter of degree. And looking at how salable are these institutions and a resolution, very limited possible acquirers for any of the institutions in these categories. And I really want to touch on the model line institutions if you think about it from a resolution strategy perspective.

If they're failing, they have some specialized business that they're involved in. And it's almost certain that's part of what's impaired. And that makes preserving franchise value through the course of the resolution significantly more difficult.

And then it's just something that we tend to see with the institutions in that category. They have more operations outside the bank chain making operational continuity more of a challenge for us in resolution. And then IDI subsidiaries of FBOs similarly operational continuity challenges.

They have relationships with foreign affiliates, with the parent in terms of shared services, shared data, shared personnel, those sorts of things. All right. So slide 16, these are some of the unique challenges that we see from a resolution perspective when considering large banks. And I would be interested to hear from the committee if these are the right considerations or if there's others that we should be focused on.

I'll quickly step through them. Here we're distinguishing large bank resolution both from GSIB resolution under Title II but also from the resolution of ordinary community banks. And in a way, they combine a lot of the toughest challenges of each plus the burden of high expectations.

I think everybody is going to remember the challenges of failing SIFIs from the global financial crisis. But for large banks, the expectations are probably closer to the failure of an ordinary bank that the FDIC tends to handle routinely and swiftly. So starting the challenges box, the first few here generally speaking relate to strategic options and the latter given to operational challenges just in carrying out the resolution.

But obviously it's touched on already. Just from the standpoint of capacity, the capital and operational resources that would be needed, there are very few institutions that could acquire a large bank. And it'll be especially difficult at the time of failure on a compressed timeline.

There's no minimum loss absorbency requirement for these institutions. Some of them do have long-term debt that could absorb losses, but there's no requirement. And that means that there could be increased costs and it could limit the strategic options available to the FDIC particularly if the depositor class is impaired.

Franchise value be destroyed and it might make it harder for bridge and sale strategies to past the least cost test. They don't have a debt structure that supports a single point of entry type of resolution. That's sometimes contemplated for these institutions.

But without that structure there, that means entry at the IDI which for these institutions is a very complex operating company for using a bridge. That means that over the weekend, it'll involve the transfer of thousands of employees and a wide array of services, assets, and contracts to that bridge institution over the weekend. I've noted the challenges with operational continuity in addition to some services being outside the bank itself.

They also just haven't fully addressed the impediments to maintaining operational continuity and resolution that some of the larger firms have and to the same degree. So next handful of challenges here, I know there are a lot of challenges which was just part of the message. Getting to the receivership entity itself, so there's a large number of deposit accounts that we would need to handle at the time of resolution for the largest banks, 10, 20, up to 40 million deposit accounts and more complex account types then for smaller banks.

So past the relationships and things like that, that would be hard to work through. And then, of course, large portions of the deposit balances are uninsured, ranging from 40 to 50 percent for these institutions on average. And then just other challenges around receivership management, the receivership entity that the FDIC would be responsible for.

It'll depend largely on the complexity

and scale of the assets that left behind in the receivership. It could be significantly simplified if we're selling the institution or using a bridge and much is moving to that. I should just note that in the event that we have to undertake a liquidation where everything stays in the receivership, the operational challenges are quite daunting in that circumstance.

The last two challenges here kind of touch on the path to failure and the point of failure. They obviously -- they have more complex business lines and the fact that we're going to need to make projections about valuations through the course of a bridge period makes our assessment of the potential cost to resolution at the time of failure more difficult. And then combine that with the fact that they're almost certainly going to fail due to a run on liquidity.

There'll be an abbreviated runway which will further reduce the time that we have to conduct valuations and to market the institution. So those are the challenges. There are a few advantages.

Importantly as was touched on the first panel, we maintain a dedicated and onsite presence at these institutions. It's hugely valuable in understanding these companies day to day. And then also in the runway to resolution when one of these banks fails, we'll have ready access to the source of technical information that we need to be prepared to resolve one of them.

We maintain two resolution-specific record keeping requirements that relate to large bank resolution. One requires these banks to be able to calculate deposit insurance within 24 hours notice from the FDIC and provide that to us within 24 hours. Another requires certain of these institutions to provide us with position level QFC data so that we can assess their derivatives portfolio, make decisions in a timely way over a resolution weekend.

And then, of course, we have an IDI-specific resolution planning requirement which increasingly involves not just the plant submission but engagement around the planning process with the institutions on an ongoing basis. So that's a lot. I'll stop there and interested for any reaction before we move on.

MEMBER MAYOPOULOS: I'm curious as to -- it seems to me that at this scale of failure, the likely cause is probably a macro event that's likely to affect multiple institutions at once. And I'm curious as to how you feel about your ability to collectively coordinate all of that and how you think about the scenario planning about what you do with one institution may impact what happens at another institution and kind of the knock-on effect of that.

MR. TETRICK: Yeah, so that could be the case, right? There could be something particular that a particular bank is doing in its idiosyncratic failure. But it could be a larger downturn and there's multiple institutions under stress at the same time.

Part of the -- and we'll get into this in the next part of this discussion. Part of the challenge here is that there isn't a built-in strategy the way that there is for GSIB resolution. And the GSIB model really relies on the resources of the institution, single point of entry.

And we're relying on sort of maintaining operations that limits the resource need on the FDIC. Now bridge strategies for a large bank can look a lot like that. The challenge is there's not a built-in exit.

So we try to focus on strategies that reduce the resource need of the FDIC. We can't control the timeline. But there is decision making with the other authorities about which weekend institutions fail on. So we would hope to not be resolving multiple institutions at the same time. But there's significant challenges and multiple failing at once.

And then just to the latter part of your question about the impacts on other institutions, this is one of the reasons why we're really focused on the impact, particularly on uninsured depositors. Because if there's a resolution that's impacting uninsured depositors and they're similarly situated banks, I think we'd be concerned about what the knock-on effects would be to those uninsured depositors. At other banks, we're seeing haircuts occur at the bank that's being put into resolution.

MEMBER ERVIN: You probably don't need any extra challenges, but I want to throw two more in. One is for acquirers. As you get bigger, a lot of regulatory tasks escalate.

So it's not just the cost of the institution. It's the cost across your whole institution where everything would be held at the higher capital and CCAR standards, et cetera. That's similarly true for foreign banks.

Foreign banks find it more expensive to operate cross border than they used to. So I think your pool of cross border buyers also is difficult. So I think in terms of what happens to buyers in this group I think is important. The second one is a legal tale. I remember a few years ago I think it was Jamie Dimon said if I tried to do this again, my board would ask me to have a psychological examination that I picked up a lot of lawsuits with acquisitions.

Those are very difficult to due diligence on in the kind of time frame you're looking at and the costs are huge. So I don't know if there's any ways you can mitigate some of those risk for an acquirer, if there any tools you have in terms of making it a cleaner institution to purchase. But that strikes me as another thing that in this kind of compressed time frame for these scales of institution could be quite difficult.

MR. TETRICK: To quickly respond, because there may be limited acquirers just in terms of capacity, our planning, we know we can't depend on an acquirer being available. So sort of looking at solutions that allow us to market an institution over time out of a bridge rather than compressed over a weekend. But we are looking at things we can do to at least expand the range of scenarios when an acquirer could pick up one of these institutions quickly. Legal risk is a good thing to look into. But there are regulatory barriers particularly for the largest institutions that would need to be overcome.

MEMBER CLAYTON: But also Ryan, I think as far as the legal risk, as we said, WaMu came on us very quickly. And everything was transferred over. We had the option to retain certain liabilities in the receivership and pay them pursuant to the priority scheme. So it's possible that we could offer Jamie Dime and a different option next time.

(Laughter.)

MEMBER O'CONNOR: I won't comment on that one. Just a couple things spring to mind. One, these large institutions -- and by the way, I should start with I completely appreciate you want to have a more prescriptive approach to getting information and creating a playbook.

But the starting point I would say is, one, you have liquidity and capital stress testing which obviously improves the shock absorbency. When I think about the Title I, Title II resolution plans for GSIBs, they were driven by, one, making sure that critical operations would continue. There would opportunity for recapitalization and to make those institutions internalize the costs of externalities they create because they created such systemic risk.

I didn't hear those components here. And I'm not saying you don't go on this path. But maybe you talk about it a little bit differently because these -- size was the other thing that jumped out, size not necessarily equaling risk.

So something big and simple, right? As long as you have the right information, you're going to be able to resolve in a very traditional sense to the way you would draw smaller scale banking institutions. So I would posit size, be careful on.

You can be a lot smaller and create a lot more complexity and be a lot more destabilizing. And then the question also I would push on, I love the recognition of model line being a problem because I think it sort of can be. But I would also say when you look at some of these small banks and the 40 to 50 percent uninsured depositors, we also have to make sure and I think you were leading down this path that if it's not systemic, those components can fail.

That's a terrible thing to say. But the reality is I think also collectively want to be careful of bailouts and moral hazards that would be potentially embedded. So I think we're on the right path of thinking about it.

Part of the wording we might want to use a little bit differently because you're not necessarily dealing with systemic institutions and forcing them to bear the externalities which is why you drove Title I, Title II for the GSIBs.

And you also have this good cushion of liquidity and capital stresses. And I would just offer up that as you think through how you present it.

MEMBER TAHYAR: I think this is very thoughtful, and I think it's good that the FDIC and the Fed are thinking about this right now. One thing to be -- we need to be crystal clear on is that the imposition of a long-term debt requirement on banks that don't have a lot of long-term debt right now in a rising interest rate environment means that you would be imposing enhanced increased today costs to solve a contingent problem. And that has to be very, very carefully balanced.

And so as you're doing your analysis on the APNR, I would hope that's a place where you would be doing a very, very deep dive. Another deep dive, thinking about the uninsured deposits which some of them might be hot money and some of them might be sticky in the sense that if it's brokered deposits, it's hot. But if it's Joe's Auto Body Shop making payroll, it's sticky. And so I would hope as you're doing the good and careful thinking around this APNR that there could be some data driven analysis around that because there's a lot of challenges to think through here.

MS. K™NIG: I have to add -- not to add challenges. I think one thing to be seen, we can see it on our side. But I think also Washington Mutual was already mentioned.

The first guaranteed to successful resolution is that it comes early enough at a point whether it's still franchise left which gets us back to the discussion we had in the first round. The second part gets us back probably to supervisory presence and realistic assessment. The second one is clearly something we are contemplating is you might not be able to find a qualified buyer for the whole thing.

But you might be able as part of your resolution planning to say there are buckets to be prepared. Now it's very simple to say they need to be prepared. If it takes two years, that's far too long.

So really in resolution planning already to think about whether there are chances to produce buckets which increase your optionality if need be without really jeopardizing the firm. And I won't comment on the question, what to do with a bank which has a balance sheet. Here is equity, there are deposits, and nothing is in between which is the challenge in this topic.

MEMBER ERVIN: But I think, for example, in Europe, you generally force MREL on banks that are smaller than GSIBs, a lot smaller, and same thing in the UK. So from an international competitiveness issue, we're in a pretty different place from other jurisdictions that have wrestled with this. I agree with Meg that this needs to be done in a calibrated way. We have a different market.

On the other hand, if we're going to internalize an externality, it is going to be a cost of dealing with a contingency. And it's a question of does that cost go to the DIF and get spread around everybody else, including the people who are behaving virtuously? Or is it internalized to the institution? That would be difficult to resolve. I would think as a matter of economics, you generally want to lean towards the latter.

MEMBER TAHYAR: And it's interesting. One of the tools we don't have here is contingent capital which is what MREL has, right? And there's been a tax blocker on that. And that may well be something that as you're going through the process of thinking through this is to rethink whether that tax blocker is appropriate.

MEMBER HERRING: I think that's a very important point because that extra layer of liability really gives you a lot more option and time in dealing with it. I'm reminded of something that the OFC did -- the Office of Financial Research did, I probably put an extra C in it -- sometime ago where they looked at the GSIB scores of all of the major U.S. banks. And

I can say from the point of view of a professional who grades, it was very nice to see a huge break point between the GSIBs and everybody else.

I haven't seen that updated now that we've had several mergers. And I'm wondering if you using those -- I'm not sure -- they're not perfect metrics but they are well recognized. If they look closer together than they once did.

But in the original cut, there was just a really comforting break between the GSIBs and everybody else. Could've been reverse engineered. I wouldn't say it wasn't.

But nonetheless, it did indicate they were quite different. If they become more alike, then I think it's a much easier sell to say we know there's a problem. We know how to deal with it, and these things should be extended.

MR. TETRICK: So as I respond to that, maybe we can turn to the next slide. If you look, there's still pretty significant grade distribution on those scores. They may have tightened some.

But I guess part of the way that we think about systemic risk is it's not necessarily binary. It depends on the scenario. And when one of these institutions is failing, if it's in the context of a wider stress, a regional bank could be disruptive.

So we've touched on a lot of this here. But just quickly and how do we think about what's the right strategy. There's not a single answer. These are the broad three approaches that we think about.

But we really focus on the middle option here, the use of a bridge bank. We've talked about why a sale to a third party acquirer would be a significant challenge. A liquidation would be extremely costly.

For a bridge bank, one thing that we're looking very, very closely at is that there's a big difference between a bridge in which we can pass all deposits in a bridge in which we can only pass insured deposits. And if there are losses incurred by the depositor class, then that makes it harder to pass the cost tests and pass all deposits. It also means that the franchise is probably significantly destroyed at that point.

And then importantly a bridge strategy, that's not an exit. That's only half a strategy. You need an exit to have a full strategy.

And so what we focus on making the bridge itself feasible and we think about some of the ways that we could exit from a bridge. And certainly being able to more readily break up parts of these institutions by lines of business, regional franchises, sales of portfolios and looking at that in advance, that's very helpful and it could help with a multiple quire type exit. We think about whole bank type exits.

Maybe over time if there's time to market out of a bridge, you can have a single acquirer. You could have an IPO type exit. And if there's significant long-term debt, you could contemplate a bailout type exit for these institutions too where you're turning the institution over to its creditors.

The problem is that the FDIC is not going to want to be in a bridge for an extended period of time. And these institutions are very large. And so executing any of those options could take a long time, and there's not a built-in exit strategy like there is for GSIBs.

And maybe I'll just turn to the last slide here. Just acknowledge there's in addition to building up our own operational capabilities to operate a large bridge, these are some of the things that we're doing to enhance large bank resolvability. Obviously, we have the IDI resolution planning process.

We're strengthening that starting with a number of submissions that are coming in this year. We've committed with the Federal Reserve to provide guidance to Category 2 and 3 institutions, so some of the largest banks that file Title I resolution plans. And then we've noted the ANPR on long-term debt.

And we look forward to seeing the comments. And those come in towards the end of the year. I think that's it on this topic.

ACTING CHAIRMAN GRUENBERG: Thank you, Ryan.

MEMBER ERVIN: Could I just make one comment? It goes back to something that Dick brought up which is, is there a dividing line in terms of the systemic risk scores? One of the things I do worry about is sort of the continuity to the U.S. banking system.

We've had our GSIBs since they got designated. They stuck there. None of them have de-GSIB'ed. And in terms of the other banks, they tend to try to stay within their buckets. And I worry that we've created some of these discontinuities, that there's no sort of ramp up that you cross a line also and you go into full Title I, planning full TLAC, et cetera.

It would seem to me that there is no bright line that really just magically separates that bank that's a millimeter over the line from one that's not quite so much over the line and that if I was thinking about a system that would work smoother, that'd be more future proof because banks want to grow and scale becomes important. That having some ramp into some of those capabilities would give you options whether to bail in on its own resources or help with a merger. That some sort of phasing in would feel like saying that both solves an industrial structure problem as well as a resolution problem.

MEMBER PETERSON: And I want to add to that that I don't think that's just based on size. It's activity based. It's broker dealers. It's international activity. It's asset management, et cetera.

MR. TETRICK: I think that's right. To Sandie's point earlier, I mean, if you just look at the GSIB scores and the sizes, there are many regional banks that are larger than some of the GSIBs. And that's because a lot of what's scoring there is the complexity of the activities, the cross border activity.

And breaking into that type of activity isn't something that the regional banks can readily ramp up into. So I think that might be part of why you don't see as much movement there. But it's definitely not just size. Size is important to us in terms of just who can acquire if you just look at it from a strategy perspective.

MEMBER PETERSON: Size is only one-fifth of the G6.

ACTING CHAIRMAN GRUENBERG: I'd like to give you all a brief break if we could. Let's take five to seven minutes. And maybe if we can come back by around 11:20 or so, we could start our last session.

(Whereupon, the above-entitled matter went off the record at 11:14 a.m. and resumed at 11:26 a.m.)

MR. CONNEELY: Okay, great. Almost everybody came back, so that's a positive. Ready to get -- okay, great. So we're on our last session of the day. We're going to be talking about CCP resolution challenges.

And there are a lot of challenges in that regard as the chairman noted up front. First we'll hear from Associate Director Jenny Traille on Title II resolution for CCPs. And then we have our guest speaker, Sir Jon Cunliffe, Deputy Governor for Financial Stability and CPMI chair. And he will over some remarks as well. So with that, I will turn it over to Jenny.

MS. TRAILLE: Thank you, John. So as mentioned a few times today, we wanted to revisit the topic of CCP resolution under Title II that we started to discuss in the last SRAC meeting in 2020. And in particular, I'd like to focus on some of the key challenges we face domestically as we think about resolving one of these institutions and highlights on the ongoing work that the FDIC is involved in internationally to address what are some common challenges across authorities and jurisdictions.

So in this session, we would like your thoughts of the prioritization of efforts to tackle these challenges that I'll describe along with any other insights that you may have and that you can share in addressing this complex but critical area of systemic risk. So many of you may recall that when we last met in 2020, we discussed the FDIC's objectives with respect to resolution, specifically to maintain the provision of the critical clearing functions in order to protect adverse effects on U.S. financial stability. We also gave a very high level overview of some of those challenges, and we would like to spend our time today going into some more detail.

So the first challenge that we face is a lack of resources that are available exclusively to support resolution. CCPs themselves have robust loss management waterfalls as part of their rule books, particularly with respect to managing member defaults. But we need to plan for it and be prepared for a situation in which these resources are significantly depleted or even exhausted by the time the FDIC is appointed as receiver.

We wouldn't want a scenario where if recovery failed, resolution would also fail. So another aspect to this issue of resources is the potential for these end of waterfall tools to have some tradeoff such as potentially pre-cyclical impacts to markets and participants that are already under stress in that type of tale event. So while the FDIC would have the authority to use the tools and resources within the CCP's rule book in Title II to the extent that they are still available, their application or the availability that we would think about in that context would be weighed against the financial stability consequences.

And unlike SPOE for GSIBs which we've talked about many times already today where we have financial resources available to absorb losses and recapitalize a firm with the purpose of allowing it to continue to perform those critical functions for the market while the resolution process is ongoing, we don't have dedicated losses absorbing resources reserve for resolution in the CCP context. Such tools have been proposed and publicly debated by legislative bodies, by regulators, academics, and practitioners. And certain jurisdictions have considered or even adopted some of these tools such as resolution cash calls that are reserved for resolution.

The second challenge we wanted to highlight which we've mentioned earlier in Jim's remarks in the first session is the lack of requirement for CCPs to file resolution plans with the FDIC. So this is again an important contrast to the bank space where GSIBs are required to file resolution plans under Title I. And in addition to providing for the resolution of GSIBs under bankruptcy without systemic implications, the Title I planning and review process as we've talked about greatly informs the FDIC's resolution planning under Title II.

So the Title I process includes firm engagement and capabilities testing which then leads to refined guidance over time and builds our understanding of the individual firm's operational options and challenges and resolution. And this has facilitated ongoing improvements in the FDIC's resolution readiness over time. And along with the benefit to the FDIC, we touched on this a bit in the last SRAC as well.

The process has also been beneficial to the firms, in particular the capabilities that they have developed as part of the resolution planning efforts have proven useful both in business as usual and in stress. The third challenge area that we want to go over today is that the FDIC does not benefit from a direct resolution engagement with these institutions. And rather we rely on the supervisory authorities of our regulatory counterparts, the CFTC, the SEC, the Federal Reserve.

And that informs our understanding of

resolvability. So this dynamic combined with a lack of Title I authority means that the FDIC doesn't have the ability to directly remove barriers to resolution or proactively enhance the resolvability of the CCPs such as requiring changes to rules, structures, capabilities, or operations. So these challenges add to the complexity of CCP resolution which I think is acknowledged as already a difficult problem.

And so we work with our U.S. counterparts and within our existing authorities to make progress. Over the last several years, we've invested a significant amount of resources together across a number of fronts. We have worked to understand how we might improve resolvability within our existing authorities to increase our shared understanding of the processes involved in a Title II resolution, including how we would make a determination for entry into resolution for a CCP and how to address the FDIC's information needs.

We've also worked to better understand

the supervisory monitoring and actions during BAU and to develop ex ante frameworks and legal documents to support resolution planning. And yet more work remains. So I do want to spend a few minutes talking about some of the work that we're doing on an international front where we're very active to further progress.

So if I could ask for the next slide. So the FDIC is very involved in international standard setting bodies such as the Financial Stability Board or FSB. We also directly engage with foreign, supervisory, and resolution authorities through bilateral and multilateral work streams.

This work helps us develop a mutual understanding of our respective resolution frameworks, address challenges across jurisdictions, and learn from one another's best practices. When we last met, we described our involvement in FSB's work on FMI resolution, financial market infrastructure resolution, which focuses on CCPs. The FDIC has played a key leadership role in that work since 2015, and we continue to be deeply engaged.

Currently, Acting Chairman Gruenberg chairs the FSB's resolution steering group. And Art Murton, the chairman's deputy for financial stability, co-chairs the working group on FMI cross border crisis management. And this work has continued over these years in a number of forms.

Over the course of late 2020 and 2021, the FSB led a series of joint workshops with the Committee on Payments and Market Infrastructure, CPMI, and International Organization of Securities Commissions, IOSCO, and Basel Committee, BCBS. And these workshops focused on the systemic risk posed by CCPs as well as the possible systemwide impacts that could occur from CCP recovery and resolution. Then in November of 2020, the FSB published guidance that laid out a framework for authorities to assess the adequacy of their financial resources to support an orderly resolution.

And this guidance is meant to help jurisdictions analyze and identify potential gaps in resources, and then consider means for addressing those gaps. That guidance then led to the chairs of the FSB, CPMI, and IOSCO committing to conduct further work on financial resources for both recovery and resolution. And in March of this year, there was a report that was published that was part of an effort to determine whether and what future policy work might be needed on the use, composition, and amount of resources.

When that was published, the FSB agreed to review the sufficiency of the existing tool kit for resolutions specifically. And considering the need for resources reserved specifically for resolution, including their associated costs and benefits, the tradeoffs that would come with those potential policy choices. And this work is currently a major focus that's led by our acting chairman as the chair of that working group with RSG (phonetic).

And then I also want to highlight that we work directly with foreign counterparts across several venues. The first that I'll mention connects nicely to our guest speaker that will come up next. And that's engagement on CCP resolution among principles from the Bank of England, the Fed, the SEC, the CFTC, and the FDIC.

This group of five agencies has met several times since 2018, including in the summer of last year and February of this year. These meetings serve as a venue for high level engagement on these unique challenges. And they serve to guide the plans for staff level work that are ongoing among the five agencies across several work streams.

We also host crisis management groups for CCPs. We talked about them a little bit earlier today on the bank space. We do this jointly with the CFTC and the SEC. And these CMG meetings or groups meet annually.

And we've had two of them since 2017.

We added a third in 20210. And we also participate in these meetings for foreign CCPs which are hosted by the resolution authorities in those jurisdictions. These meetings are valuable meetings to understand our shared challenges, share approaches and progress, and try to identify improved resolution options. So with that backdrop, I want to turn to our chairman to introduce our guest speak who has graciously agreed to speak today and address questions.

ACTING CHAIRMAN GRUENBERG: Thank you, Jenny. That was very helpful. We wanted Jenny to sort of lay out that background and context before we turn to our guest speaker, Sir Jon Cunliffe.

I suspect some of you may know Jon. He serves as the Deputy Governor of the Bank of England for financial stability. He's also chairing as Jenny mentioned the Committee on Payments and Market Infrastructure for the BIS. He's really been an international leader on payment system issues and has particularly focused international attention for several years now around the risks related to both the supervision and the resolution of central counter-parties.

I think of all the issues relating to the resolution of systemic financial institutions since the 2008 crisis, this is the one that really stands out as clearly a profound system of consequence in which we've arguably made at least progress. There are a lot of reasons for that. Perhaps Jon will talk about that.

But I couldn't think of anybody better to at least give us a broader perspective on what I do think is a fundamental systemic resolution risk for the FDIC and for this committee to engage in. I would note that prior to taking over his payment system responsibilities, Jon had also been responsible for the resolution work at the Bank of England. So Jon and Elke and I collaborated very closely on the cross border working relationship on the traditional GSIB resolution issues.

And in some sense, we're now continuing that on the CCP work in Jon's current capacity. And I would note Jenny mentioned the US/UK working group on CCP resolution. I always envied Jon at those meetings because on the U.S. side we had the Fed, the FDIC, the SEC, and the CFTC and on the other side was Jon --

(Laughter.)

ACTING CHAIRMAN GRUENBERG: -- basically embodying all these authorities and thinking to myself, boy, his life may not be easy but it's at least a little simpler than ours. So with that, I think Jon is on the line. And we can ask him to offer his remarks. Jon, thank you so much for joining us today.

MR. CUNLIFFE: No problem. Thanks, Martin. First just to check whether I'm audible and visible.

ACTING CHAIRMAN GRUENBERG: Yes, both are true.

MR. CUNLIFFE: Okay, thanks. And secondly, apologies. It's a privilege to get a chance to address this group. And I would've liked to have been there in person, but I have a meeting tomorrow morning in Basel which we'll among other things talk about the work planned for CCPs and non-default losses and the like.

And it made it just impossible to be with you and to get back in time. And as it's nighttime in Switzerland, I'm afraid I may look a little -- the lighting may look a little strange. So I apologize for that as well.

Just a quick word about what I do. So I'm Deputy Governor for Financial Stability. But I also have responsibilities for CCPs, settlement systems, and payment systems for the supervision and regulation.

So I'm both kind of micro-prudential and macro-prudential in this area. And up to a few years ago, I also had responsibility for resolution. One of the reasons I gave that up to another deputy governor actually was because we thought it was bad practice to have the same person responsible for supervisor and for resolution. I think it's good practice for those things generally to be split.

So for today's perspective, I guess I'm speaking from the perspective of the FSOC from a financial stability perspective and the CFTC and the SEC and CCP regulator perspective. And I'm not speaking from the perspective of the FDIC. But I can still remember resolution --

(Laughter.)

MR. CUNLIFFE: -- work. As Marty said, I also chair the BIS Committee on Payment Systems and Market Infrastructure. And more importantly, the joint committee with have with IOSCO which functions as the standard setter -- the international standard setter for CCPs and issues the PFMI which are our version of the Basel standards for CCPs and settlement systems. So I thought I'd start today with all my hats on and then speak from different perspectives.

But I'll identify when I'm talking from a UK perspective. And I apologize again in advance. I don't know how much of these issues you covered in previous discussions, so some of what I say may seem blatantly obvious in which case talk amongst yourselves or something.

(Laughter.)

MR. CUNLIFFE: If I lose people, I'm happy to pick things up in questions. I'll set out briefly why we need effective regimes to deal with CCP failure, why CCPs are different than banks, and the risks they take and how they manage them, and what the UK regime will do. And we have proposals for a new regime which are now in front of Parliament which I hope we'll get Parliamentary approval and we can start to implement early next year.

And in doing so, I'll touch on some of the suggestions that have been made for CCP resolution. So first, what does it matter? Well, as we know, CCP's role as central nodes in the financial system have made them if they're large enough naturally systemic and they protect key markets from counter-party credit risk.

And we saw what a failure in that area

can do during the great financial crisis. And by mandating use of CCPs for some key financial derivatives after the GFC, we've made some of them even more systemic globally. For example, 60 percent of credit derivatives are now -- swaps are now cleared centrally as opposed to 10 percent before the great financial crisis.

Eighty-five percent of interest rate contracts are cleared by CCPs. It was about 40 percent before the financial crisis. And of course, that's just the proportions.

The actual quantum has grown as these markets have expanded pretty significantly. And just as important as financial markets, we've seen the role of CCPs in commodity markets and in terms of the recent stress and the role they play in enabling hedging and forward contracts. So CCPs represent a concentration of risk.

I always say this. That is not some unintended consequence after the great financial crisis. I mean, the assessment at the time is the benefits from centralization in terms of consistent and prudent margining, transparency, netting, and the mutualization of losses made central counterparts clearing preferable to a complex and what would be a peak wave (phonetic) of bilateral contracts with much larger gross margin flows.

That was the decision we took back in 2009. I think it still holds, but we can't ignore the concentration of risk and the failure of a CCP and the effects that would have. And it would transmit stress quite widely throughout the financial system.

And it would remove the protection against counter-party credit risk which I think is essential for markets to operate. So we do need to find effective ways to manage a CCP failure. And because the concentration effects exist, it means actually there are returns to concentration in being a CCP which means many of these businesses are global and they meet international standards in the same way as we need international standards -- strong international standards for the resolution of globally systemic banks.

However, and it's an important point, CCPs are not banks. And the design of any resolution framework I think needs to reflect some of the essential differences. The first and most obvious, the risks they run are very different.

They don't do maturity or liquidity transformation. They don't have complex balance sheets with asset and liability structures or mismatches that need to be resolved. The two risks they face essentially are counter-party credit risk, and we'll talk about that, and operational risk of some sort of operational failure.

On counter-party credit risk, I mean, this stems from the default of one or more of their members. As their function is to be the central counterpart, in other words, to stand between the two parties to a trade, they really have to ensure at all times that they have exactly offsetting contracts with the buyer and the seller. In other words, they have to maintain matchbook at all times.

And if one of the counter-parties defaults, they need to be able to absorb the losses that will probably be necessary to restore that matchbook by finding contracts to offset the contracts that have been lost. Now unlike banks, they don't hold capital really to absorb loss absorbing capital. Rather under their rule books, they can effectively pass losses with limit back to their clearing members.

First they do that and I think the previous speech I mentioned the waterfall of allocation of losses. First they do that by using the pre-positioned resources of the defaulting member. And then they fail to neutralize the losses by using the pre-funded default fund to which all members contribute.

And then when the pre-funded resources run out, they have the ability to make cash calls on the remaining members. And then after that, they can start to haircut the margin they owe to some of their members. And finally, they can tear up some or if necessary all of the contracts they have with their members.

So actually, unlike banks, when it comes to default losses, CCPs can't go bankrupt. At the end of the waterfall of recovery actions, they just tear up all the contracts and effectively the clearing service disappears. And I should say that if you follow the rule book, the equity of the others is untouched in that process.

But of course, from a financial stability point of view, those clearing services are important. And tearing up of contracts removes the hedges that counter-parties will be depending upon in stress. So the CCP service needs to be kept operating and the transmission of stress needs to be kept to a minimum.

So a quick word about non-default losses. The other main risk is operational losses not caused by default, fraud. It could be cyber. It could be investment losses.

Here CCPs generally have no powers to pass those losses on to their members. Non-default losses have to be absorbed by CCP capital. And CCP capital is generally pretty small relative to the size of their operations.

For one of our big CCPs, their capital is 500 million euro. Their default fund is ten times that. The open interest passing through the CCP is many, many times greater.

So non-default losses could therefore wipe out the capital of the CCP and lead it to insolvency. And the result again would be the loss of the clearing service. So how should resolution address those risks?

Well, the first point to make is that even though for default losses, the CCP rule book means it can effectively wind itself up without bankruptcy. The latter stages of that waterfall process could be systemically very damaging in the allocation of losses across the wider financial system, particularly when one comes to the tearing up of contracts. And clearly as I said earlier, poor financial markets could disappear if we lose effective clearing services.

And in following through those recovery actions, CCP managements have choices they can make in how they carry out those actions. And there are some actions they can't do under their rule books. And to some extent, they're tied to the secrets of actions that the rule book sets out.

And the last point to make that as they carry out those actions, it's very likely that there'll be disagreements between CCP management owners on the one hand and clearing members on the other. And we've seen cases of that with defaulting members in some instances in CCPs in the past. So my first point is it is imperative that the resolution authority can step in and take control before CCP recovery actions are exhausted.

I think the earlier speaker made the point that you want to ensure that when you get to resolution the resources or the options that are available have effectively been exhausted. So for us, one key issue is the resolution authority needs to be able to step in on failure or the likelihood of failure before recovery actions have been taken too far. And the resolution authority needs to be able to use the CCP recovery tools flexibly.

But where those are sufficient, it needs to have extra tools that it can use outside the rule book. And of course, it needs to understand to do this and to step in that way, it needs to understand the business of the CCP. And there needs to be a resolution plan that has agreed in advance.

And resolution authorities I think can then take actions, most of which will be in the CCP rule book. But they can take them with the view to the avocation of losses across the system in taking into account financial stability considerations. And then, of course, resolution authorities will operate within a public law framework.

And I think one of the points has been made to us by the private sector is that would reduce once a resolution authority steps in. That reduces these tensions between CCP management and owners on the one hand and members on the other. And of course, in all of this, it's important as with other forms of resolution that there is a robust no creditor worse off provision.

And the counterfactual in this case is I think should be what would happen if the rule book had been followed all the way to the end of the waterfall? So the current UK regime -- we have a regime, we have one in place since 2013 -- has many of those features. But it doesn't have them all.

And the legislation that's now going through Parliament I think will give us all of those powers to operate ex ante, to require resolution plans, to remove obstacles to resolution, to step in when we need to step in.

And then it will give us in some areas some extra powers that don't exist in some of the CCP rule books. And it will ensure that no credit worse off provision in the way that I described it.

This raises the question, though, for default losses is do we need extra pre-funded resources either in recovery or resolution to supplement what already exists. And I think, Marty, this is really where your resolution group is now focusing. So seen from our perspective, there are two reasons why you might want to increase the pre-funded resources in the CCP waterfall.

The first and this is a key issue for us is the question of incentives because our CCP equity is not going to be written down. In the case of default losses, do CCPs really have the right incentives to risk manage properly, particularly when they're in competition as many are internationally with other CCPs? And a point that's raised by the private sector is whether the allocation of losses between members on the one hand and CCP owners on the other is unfair because it's very little CCP skin in the game when the losses are mutualized.

So it's for that reason that some jurisdictions like the UK already require CCP owners to have skin in the game. It's not equity, but it's pre-funded resources that can be called upon as mutualization takes place -- mutualization of losses takes place in the waterfall. And the issue is how large that skin in the game should be.

Kind of what stages of the waterfall should be exposed to loss? The UK regime that's now being legislated will give us the power to call for a second skin in the game tranche which we could insert at a later point in the waterfall. But the key point here, I think -- and the size of that is something we have yet to determine.

But the key point here to be clear, the objective is to ensure that the incentives are sufficient and rightly placed to avoid resolution by incentivizing CCP management. It's not really a question of ensuring the pre-funded resources are available in resolution. So that's the second reason you might want to increase pre-funded resources to ensure that you have enough in resolution and that you don't want to rely on cash calls, haircutting the variation margin, or in the later stages tear up once the resolution authority comes in.

So one option which has been much discussed, pages written about this, would be for CCP to raise extra resources by issuing bailout bonds in the way the banks do. And then those bonds could be written down in resolution and the funds used to absorb losses. So a number of reasons have been given as to why that might be preferable to depending on the cash calls and cutting of margin and other tools.

One is whether cash calls will be too procyclical in the event of CCP stress. And it would be better to have the resources pre-positioned. And the other is whether cash calls will actually be effective because clearing members might want under stress resist further cash calls.

And this is a kind of complex debate. And I think it's going to be where Chairman Gruenberg's international group go next. But I thought I'd offer a few thoughts on this. And it's informed, in part, by the first stage of the international work which looked at the sufficiency of pre-funded and non-prefunded resources in a number of systemic CCP's ability to absorb losses and recovery and resolution. And I think that work was published earlier in the year.

And the work suggested that these systemic CCPs could absorb failure of up to four of their largest clearing members. And the international standard is two large clearing. But they can absorb failure up to the four largest clearing members, although some would exhaust pre-funded resources and need to go into cash calls at that point.

But the cash calls that will be necessary would be within the capacity of the remaining clearing members which tend to be the larger financial institutions. And on the question of whether firms would be able to resist cash calls, I'd only observe that if you resist a cash call you're effectively in default. And that triggers other default cross causes.

So I think it's unlikely that clearing members would try to resist contributing to cash calls. But there's a big caveat in all of this which is in a (phonetic) in which, say, three to four of the biggest clearing members fail, we may find that actually those liquidity resources aren't available for the other clearing members. And this could make the stress more stressful.

And the only points I'd make, though, is if we're in a stress in which three to four of the big clearing members fail, remember that's not just in one CCP. That's across the board and across the financial system. And if the resolutions that we're talking about potentially the failure of, say, two to four GSIBs.

And then the resolution arrangement for those GSIBs has also failed, the resolution would enable them to continue to meet their obligations to a CCP without default. I think we're going to be in a pretty heavy systemic crisis and bailout bonds and the resources that they might offer, even if it's a full reload of the default fund may help. But they're likely to be able to resolve the systemic issues that we face.

And those considerations I think need to be balanced quite carefully. In the end, it's a question of how far into the tale of the risk distribution you want to go with protection. And does the extra bang that you get by, say, bailout bonds, is it proportional and do the costs outweigh the benefits?

And I'd say that there are costs which we need to recognize. Just a simple thought experiment back of the envelope. If a CCP issued bonds equal to the default bonds, so it would have a full reload in resolution.

The annual coupon of that could be equal to or greater than CCP capital. And those costs, of course, are likely to get passed back to users raising the cost and reducing the incentives to clear. So one needs to think about benefitting that sort of systemic stress you will get from this against the costs and the disincentives to clear in business as usual.

Of course, jurisdictions are different and there could be jurisdictional reasons why one might want to go at least some distance down that route. And in a world where the resolution authority either doesn't have the line of sight or can't effectively or quickly step in before the resources that are available in recovery are exhausted or whether the resolution authority is not able to plan for CCP resolution and for the comes in and has to deal with a very complex situation without there being a plan or sufficient advance knowledge or where CCP rule books are either -- they don't provide sufficient options or actually there are obstacles to resolution there which can't be cleared away. In those circumstances, one might argue, well, a reservoir of pre-funded resources that can be accessed only in resolution might be necessary to enable CCP clearing service to continue to operate.

The next stage of the FSP work will look at these issues and maybe tease them apart and give us better line of sight. And finally, and I'll stop here shortly, just I should say a word about non-default losses because in a way these are equally if not more worrying because the position is very different. And the CCP recovery actions are very limited.

And the capital to absorb these losses is pretty limited as well. So the resolution authority in that case will not be able to depend on the waterfall. It will need to have access to some other resources.

So in the UK, the new powers that we hope will be approved by Parliament will give us the power to make a cash call. We're thinking of something proposed to be put out there. It's three times the default fund to cope or to absorb the losses of -- non-default losses and to recapitalize the CCP.

And of course, if those circumstances, there is no credit or worse option, well, protection that protects the equity. And so the equity of the CCP will be wiped out. We need to think about what then happened to ownership and whether the CCP was passed back to the members.

But we feel it very important in the UK there is a resolution authority. We have access to resources, the deal with non-default losses. Now bailout bonds could be a reason to do that as well.

But as I say, the cost of holding them is high. And of course, if it's an idiosyncratic failure of the CCP because of fraud or cyber, then we won't be in a systemic crisis. And those cash calls wouldn't have that procyclical effect. But again, that's how you deal with non-default losses as a resolution authority needs to be worked out.

And I think it's very important a resolution authority has access to some resources to meet that and to be able to keep the clearing service in operation. And the last point I'd make and this is something that will come up in our meetings tomorrow, of course the CPMI-IOSCO standards are for the operation of CCPs. They don't include resolution. We deal with life and the resolution authorities deal with that (phonetic).

(Laughter.)

MR. CUNLIFFE: But I think we need to think about in recovery should CCPs have better options to deal with non-default losses. And that's work that I hope we'll be starting in the future. I'll stop there, Marty. Thank you.

ACTING CHAIRMAN GRUENBERG: Jon, thank you very much for that. I must say exceptionally lucid presentation on a pretty complicated subject. And Jon's agreed to take a few questions from the committee if there any members that would like to follow up with him. Yes, Dick Herring from the University of Pennsylvania for Jon's benefit.

MEMBER HERRING: Thank you. That was a terrific overview. You didn't mention one of the differences from a bank resolution that strikes me as very important in this case. In a bank resolution, we can hope at least to have a resolution weekend. It strikes me that with a CCP, you have almost no time to intervene and try to take control of the situation, keep it from deteriorating quickly. How do you deal with that much shorter time for action?

ACTING CHAIRMAN GRUENBERG: Jon, I think you may be on mute.

MR. CUNLIFFE: I'd been on mute. I'm sorry. Look, that's a real challenge. And in the circumstances which this is happening and say two clearing members have defaulted, prices will be moving very fast in markets. And so you'll be in a situation of general stress.

We've -- I mean, to my mind, it makes the case for the resolution authority to be closely involved with the business of the CCP for there to be close cooperation between the CCP supervisors and the CCP resolution authority. It's easy for me to say that because in the Bank of England we look at these things in an integrated way. But also the resolution plan has got to have stabilization.

That said, some of the defaults we've seen in the past, CCPs have been able to go through that default waterfall quite quickly. I'm thinking of Lehman Brothers. So the Lehman Brothers default. There were large positions held certainly at the London Clearinghouse.

And those positions were closed. They were auctioned off, the losses absorbed in the middle of a global stress if you remember. The losses absorbed and people paid out very quickly whereas the nonessential clear contracts took years to work out in a bankruptcy.

But it is a challenge. I think what

we'll do in the UK also is we will do some dry runs and some kind of resolution testing. I think that once the resolution authority steps in, we haven't had to do a big resolution in the UK I'm pleased to say.

But once the resolution authority steps in and says, look, we are now in charge. We're taking over control of the rule book and the actions, I think that might also have a stabilizing effect. But ex ante planning, wargaming, knowing where your tools are and the risks I think will be essential. But it will be quite a stress period.

MEMBER HERRING: Thank you.

ACTING CHAIRMAN GRUENBERG: Wilson Ervin?

MEMBER ERVIN: Thanks, John. I agree. This is a terrific presentation on a tough subject. We recently gone through a period in a few markets where interest rates were quite shocked and went outside some of the initial margins that people had been thinking about.

I am wondering if we're thinking about different types of events where we might want to protect, could minimum initial margins, some sort of constraints on that be another solution if we're thinking about different types of waterfalls that could internalize more of these to the stressed members and take some of the pressure out of this. A second question I had is if you're not wiping out equity in some of these cases, how do you align the incentives of the CCP towards systemically positive events? If it's really not coming out of their pockets, how do you improve that alignment going forward?

MR. CUNLIFFE: So on the first, I think, I'm doing work with IOSCO co-chairing a group with Ros Behnam of the CFTC on what we saw in the dash for cash in 2020 and actually what we've seen in the commodity markets. I should say, by the way, if that was a polite reference to the little local difficulty we had in long gilts in the UK a couple weeks ago, those are all bilaterally margined. So we didn't actually --

there was no CCP impact.

The impact was taken by the banks that were providing the repo basically and margining bilaterally. But more generally, I think we do need to look at the responsiveness of CCP margin to shocks. And I mean, this goes down to the unlovely name, do you need mechanisms for anti-procyclicality.

So in other words, should we be calling margin more prudently in good times or normal times so that the jump to stress margin is not so great in their terms. And we will be looking at that work. We published a report in that group.

We just looked for the dash for cash, and I'm hoping we can look at that internationally, at least some interest to look at the responsiveness of CCP margin models because ideally as we've been, so more than ideally, you don't want to be in a resolution situation to begin with. And the protection against default losses is the initial margin that the defaulter has to pay in advance and then the sizing of the reporting. And I hope out of that will come some views on how to measure procyclicality of margin and stress which is what will cause the default.

The margin would go up. You will see the clearing member will not be able to pay. And do we need to -- I think you called it minimum margin. But do we need to be calling a bit more margin in normal times a bit overprudently in order to avoid a big jump under stress?

Some jurisdictions already in the UK and Europe have, I'll use the word, anti-procyclicality measures. We learned some lessons in the dash for cash about how effective they are. But I think that is an issue. It's one answer. The other answer to avoid you getting to resolution is exactly as you said, making sure the incentives are aligned.

The problem with equity, this is something I think the FSB wrestled with when it put out its first set of guidance some years ago is if you have a no creditor worse off protection and if the rule book basically says the CCP can call of them to make unlimited calls on its members and then wind itself up and still preserve the equity. You can't square that with writing down the equity and resolution with a no creditor worse off guarantee. I think that's something that needs to be looked at again actually. And we need to think about whether the no creditor worse off guarantee should offer that level of protection to shareholders in terms of incentives.

But skin in the game, so resources which are not equity don't go to the ownership but which belong to the CCP owners and which are exposed either initially when mutualization happens or initially and then as you dig deeper into the waterfall, that's one way of if you like creating the incentives that writing down the equity would give you without having to wrestle with this no creditor worse off protection which is important in resolution because we are disturbing people's legal property rights and they do need to be protected. But I think incentives will be part of it. And certainly in my jurisdiction we're going to be looking at skin in the game and whether that is in the right place.

ACTING CHAIRMAN GRUENBERG: Yes, Sandie?

MEMBER O'CONNOR: Jon, thanks so much. A few just sort of follow-ons. You talked a little bit about the non-default losses and having the resolution authority have the ability to cash call. Again, just how are you thinking through because you clearly know that's the risks that are occurring are solely brought on board by the CCP management itself.

And I should say we're talking about deneutralize, not neutralize CCPs. But they make the choices on where to place their investments, where to place that collateral, and how much they spend on their cyber resilience. So having the backstop of doing a cash call of the clearing members which have no engagement in that risk management but provide a pocket.

Well, I understand that can stabilize. That's just such a disconnect. How can that be a good long-term approach? And maybe you're saying that's why we want to look for better tools to really aligning incentives to appropriate risk management. That would be the first question I have. And I have another one if I could, Chairman.

MR. CUNLIFFE: Let me do that one. Should I do that one because I'll --

MEMBER O'CONNOR: Please.

MR. CUNLIFFE: -- forget.

(Laughter.)

MEMBER O'CONNOR: Me too. It's all good.

MR. CUNLIFFE: Yeah, so look, I mean, before losses start, there is a really big problem, we already have actually in the UK that you can mutualize the investment losses where they put their money, where they put their margin, where they lose that. So we already have that in the UK regime, but we'll extend it. I think you're in the world of second best here.

Bear in mind that however you fund that, whether it's pre-funded resources or whether it's a cash call, have a clearing obligation, clearing mandate on many of these services. Those costs are going to be passed back to users. So it's not a question that there is some way that users can avoid the costs.

If you say we -- and of course, with non-default losses, it's very difficult to size them, particularly something like a cyber attack. But if we said, like -- the idea I think has been talked about in the UK that it's a multiple of the default fund. The carry cost of that is pretty large, and it's passed back to the members.

Now of course, these resources, they're not doing anything because they're just sitting there kind of waiting to be used which is a difference I think with banks (phonetic). So in that world of second best, I think you wanted two things. Non-default losses would wipe out CCP equity.

There's no, no creditor worse off protection there because in the current rule books that's what would happen. So the incentive has to come from the wipe out of the equity which you think would have some incentive effect. And then I think members will be -- members need the clearing service, and we need the clearing service to continue.

And the choice then is because these are multilateral. You go back to the members or whether the public sector steps in. And I think public sector support, but CCPs are something we all want to avoid for the obvious reasons.

And so one last thing which is as we back resolution in the situation where CCP's capital is wiped out by the members. And then the losses are absorbed by the cash call, and the CCP is re-capitalized by the cash call. Then in those situations, the members would then owe the clearing services.

I mean, they might not want to, but that's pretty much the same as in bank resolution. But I don't think there's an easy answer to this. One better answer to this I think might be for CCPs to have better recovery options and also to think about how would their members, they manage these risks.

As a general view, think the more you put members -- expose members to these risks, the more they will demand, I think, more involvement in risk management and to understand what is to be expected on CCPs. And maybe that comes to something around the governance of CCPs and the governance of risk management machinery. Just one last point on that which -- I'll get told off for saying it, but I'll say it anyway.

When you talk to the CCPs, they tell us that the pressure they get from their members is to charge less margin, to reduce the cost of failing all the time. When you talk to the clearing members at very senior levels, they say they're worried about the risk in CCPs and the fact that they are exposed to these risks, both the neutralized default and the non-default. And they don't have kind of enough influence on the CCPs.

I think some of the answers to this lie in the clearing members. And actually whether the risk controlled impulse in the clearing member outweighs the can I do this trade as cheaply as possible impulse in the clearing member. So there are some issues there, I think, for clearing members as well.

MEMBER O'CONNOR: Yeah.

MR. CUNLIFFE: So you had a second question.

MEMBER O'CONNOR: Yeah, let's -- so well, I think just a couple things. I think on the governance, I think you nailed it there. And I think if you see many of the writings and the acting chairman mentioned them by both buy side and sell side, I think there's just a very clear drive by global industry -- and I'm no longer in it anymore -- to actually build up front resources because you want them to be predictable, manageable, and understood. Yet it seems really hard to get there. And I'm just curious as to your viewpoint because it seems like our regulators are aligned. Our academics are aligned.

The industry wants something yet we are not there yet. And I think up front is the way to go and inclusive of bail-inable debt except I would just offer rather than shock absorbency, that's really your recapitalization mechanism, right? Because then it moves from a demutualized to a mutualized model which is probably a more appropriate model.

But that's just not where we are at the moment. So I guess my question is why are we collectively having a hard time if everyone says they want more pre-funded, they want TLAC, they want better collateral, they want more appropriate through the cycle margins. So I'd love your view because I certainly can't figure it out.

MR. CUNLIFFE: So first of all, I think to the extent the CCPs complete a margin that they shouldn't. So I don't know if they do or not.

MEMBER O'CONNOR: They do.

MR. CUNLIFFE: But to the extent they do, that's because they're under commercial pressure from their clearinghouse. And when you talk to them, particularly for clearing services, there's a contest between different CCPs. We certainly get an awful lot of reports that they are basically under pressure because they're clearing members will go to the cheapest auction and of course pre-funded resources cost money.

But there are other things that cost money in terms of margin as well. So I'm not sure it's quite as one sided as one things. And of course, the cost of bailout bonds as I say, so I think the report from London Clearinghouse is around 10 billion.

I don't know what it will be on the

bailout bond. But that cost particularly where there's a clearing mandate and they're legally obliged to use the CCP. And they just want to get into the economic regulation of CCPs. Maybe we'll have to go there one day.

Those costs are going to come back to members as well. So I don't see this as such a one side set of issues to be honest. I think there's a really big issue about transparency. And this comes down to margin models.

One of the recommendations of the CPMI-IOSCO group as I mentioned was that there should be much more transparency around margin models and their procyclicality, how they will react in stress so that clearing members can see that and plan for it. But also metrics so that clearing members can have a view on whether they want to use CCPs with more procyclical models or less procyclical models. Some of it will depend on the nature of the clearing services.

Clearly a great difference between clearing agricultural futures on the one hand and interest rates on the other. But I think transparency is a big issue here. But I think also we need to think -- individual regulators needs to think about whether I called it pre-funded or whether I call it just the way those margin models attune between pre-stress and stress.

I think there's a conversation to happen as well. But I mean, I guess my point is at the end some of the pressures on CCPs come from the members. I think it would help if members looked to the seniority and the background of the people they appoint to those committees.

MEMBER O'CONNOR: Yeah, I think you're right about that. And I would suggest to that where members -- clearing members raise certain issues that are related to risk, whether it's margin or collateral or things of that nature. There's a way that those that oversee the CCPs have insight into that because I think there's a gap between what the clearing members may weigh as a viewpoint and whether or not that gets taken on board.

Reference, Don and I wrote a little bit about this in the Task Force on Financial Stability in December 2017 when Bitcoin went on to CME, for example, and got part of the waterfall in the default fund. That's interesting, not standardized, et cetera. So I just think we need to create some transparency there so that the regulators can be actually helpful in understanding the risks that are coming on board.

MR. CUNLIFFE: I think that's right. But I think the regulators also need the power to be able to take those decisions. And different jurisdictions have regulators who have different powers for the approval or not of new clearing products.

But some of this goes, I think, to regulator and supervisible powers (phonetic). And it's not just new products. And there's also actually part of the legislation I was talking about. We'll give the Bank of England rulemaking power in this area which we haven't had in the past because it was all done in euros. We have to have more options, I think, in the future.

ACTING CHAIRMAN GRUENBERG: Good. Are there any other questions for Jon?

(No audible response.)

ACTING CHAIRMAN GRUENBERG: Jon, thank you. This has been a superb overview of an important issue. And we want to elevate attention to it, so this will be an ongoing issue and matter of attention for the FDIC. And we'll bring it back to this committee as well. So thanks a lot.

MR. CUNLIFFE: Okay, thanks. Thank you for the invitation, Marty. Also, thank you for taking on the international work. These are basically global infrastructures and we need to manage this.

ACTING CHAIRMAN GRUENBERG: Thank you. We'll see you. All right. Well -- yeah, John.

MEMBER REED: It was interesting, the

contrast between the Bank of England. I got the sense from our earlier discussion that most of the progress we've making here is procedural. We've got a lot of people talking together and building understanding that we didn't have before. But substantively, where do we stand here in the United States if one of these units were to get into serious trouble. Do we have the capability to deal in a timely way?

ACTING CHAIRMAN GRUENBERG: I'll be glad to respond, but I'll give Jenny first crack.

MS. TRAILLE: Sure. So I mean, we've highlighted a number of the challenges today, including the runways likely to be short. So I think that we look at the existing planning that we have, our existing authorities and tools. We talked a lot about the procedure, the way we work with the supervisors and the other authorities because that's how we build our understanding and our information.

And so we do look at individual firms and we do build on that planning. But we acknowledge that there are challenges and there's more work to be done there, data. I mean, there's a lot of things that we've highlighted.

I think ultimately the strategy for CCP resolution isn't that much different than what we would attempt to achieve in further institutions in that you're trying to preserve those critical operations for the market. And so if there was a -- we would look to move those critical operations into a bridge institution. And so the work then goes into how do you operationalize that. But the strategy isn't so much different. It's just all sort of the unknowns and the information that we need.

ACTING CHAIRMAN GRUENBERG: If I can comment, and it really goes to the broader issue that was raised earlier about the gap on the resolution side relating to non-bank financial companies of which CCPs are in some sense the ultimate example of a systemic nonbank financial company. And the fact is this is my perspective on it that the Dodd-Frank Act really put in place a coherent framework of authorities for the agencies to deal with the resolution of a global systemic banking organization. We really have the Title II authorities with the orderly liquidation fund backstop complemented by the Title I resolution plans which gives us both a line of sight into the companies and authorities to get the firms to make organizational and operational changes to enhance their resolvability.

And we got domestically and internationally an agreement on a requirement for TLAC additional loss absorbing resources to facilitate the resolution of the firm. So that we really have a -- and we've made enormous progress if I may say in terms of cross border cooperation with the key jurisdictions represented by Elke's presence here and Jon's participation in this meeting. So that we've really built what I would consider to be a fairly credible framework which hasn't been tested yet in practice.

We have not yet executed it. So I have that caveat that until we do it, I'd be a little cautious about what representations we make. But I think we have a set of authorities, capabilities, resources that did not exist across international relationships that simply didn't exist prior to 2008 that puts us, I believe, in a very different place.

And then I happen to believe we could execute if it were required of us. I think in the nonbank financial company sector and the CCPs are the prime illustration of this. We don't have that coherent framework.

And I should mention the supervision authority that we talked about earlier where we as the banking agency have a supervisory role and line of sight into these firms. On the nonbank side and CCPs are a good illustration, we have by default Title II would be the public authority for a systemic firm failure, whether it's a bank or nonbank. And we can bring those authorities to bear.

But the supervision responsibilities are in the market regulators. And we do not have a resolution planning requirement. And we've just been -- we're talking about internationally additional resources, loss observing resources, and resolution but don't have something in place.

So we don't have the framework on the nonbank side including the CCPs that we've built on the banking side. We have the benefit of now having a framework and an example to learn from and apply. But frankly, we have a lot of work to do in the United States with our counterpart agencies to try to as best we can the Fed, the SEC, the CFTC to try to collaborate in the absence of additional statutory authority as well as on the international side to try to build stronger cross border relationships.

But the question is a fair one. We don't have the framework, the infrastructure in place on the nonbank side. And that's why this is on the agenda for today's meeting because I think looking at the post-crisis world, this is probably where our attention and priority needs to be.

MEMBER CLAYTON: Yeah, all I can say is I agree with you. Back in my old seat, both of these conversations that we've had today are related. Who are the members of the CCPs?

They're the entities that we're looking at. And I knew that if it's a broker-dealer, you would be calling me, telling me make sure they make good on their obligations to the CCP because they have to be related, right? They can't look at CCP resolution in isolation from resolution of financial institutions because they're going to happen at the same time.

MEMBER O'CONNOR: And the great news is in most of the financial institution -- I think in all of the financial institution resolution recovery plans, their exposures to the CCP are in there, right? And their largest counter-party exposures are in there. Where I think the model becomes less stable from the centralized approach is these uncapped cash calls, these potential contract tear ups which is basically taking the CCP out of the space of being a CCP and opening up exposures that people can't manage.

And just to follow that thought through, if you're a clearing member, you're not allowed to operate out of a CCP. If you're an end user, you can go. But who are you going to trade with because there's no market debt?

So these are -- again, if they're predictable, manageable, it can be done. Those pieces need to be closed down. And the last bit I think we should carry on thinking about is, who has some of these extraordinary tools?

Who can enact them, like, variation margin haircutting? And for those who may not be as familiar with it and I'm sorry to say I am as familiar with it as I am. That would be the equivalent of in a bank resolution plan saying we are just going to haircut your deposit in order to survive.

That wouldn't exist anywhere else. So

if we're going to think like that, who does that and for how much? Because that might be perfectly good in recovery for a recovery and resolution authority to do.

But I would question that in the hands of the management of the CCP that has taken it into this place. And again, the demutualized model, not the mutualized model. So I think that's where the work needs to be done.

And the reason hair is not on fire is because we do have a lot more strength in our CCPs. There is margin. We saw the results of the recent report that came out at 4 times coverage and 1.4 times scale up, right?

Those are good things. But time, we need to sort it out it seems to me. So really please keep doing this really important work so we can finish taking it to the hoop.

ACTING CHAIRMAN GRUENBERG: Thank you. Anything else for today?

(No audible response.)

ACTING CHAIRMAN GRUENBERG: Well,

thank you all. This has been a very helpful discussion, and we appreciate you all taking part. And we'll do it again next year. Thank you, all. And we'll have lunch upstairs.

(Whereupon, the above-entitled matter went off the record at 12:33 p.m.)

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C E R T I F I C A T E

This is to certify that the foregoing transcript

In the matter of: Systemic Resolution Advisory Committee

Before: FDIC

Date: 11-09-22

Place: Washington, DC

was duly recorded and accurately transcribed under my direction; further, that said transcript is a true and accurate complete record of the proceedings.

Court Reporter