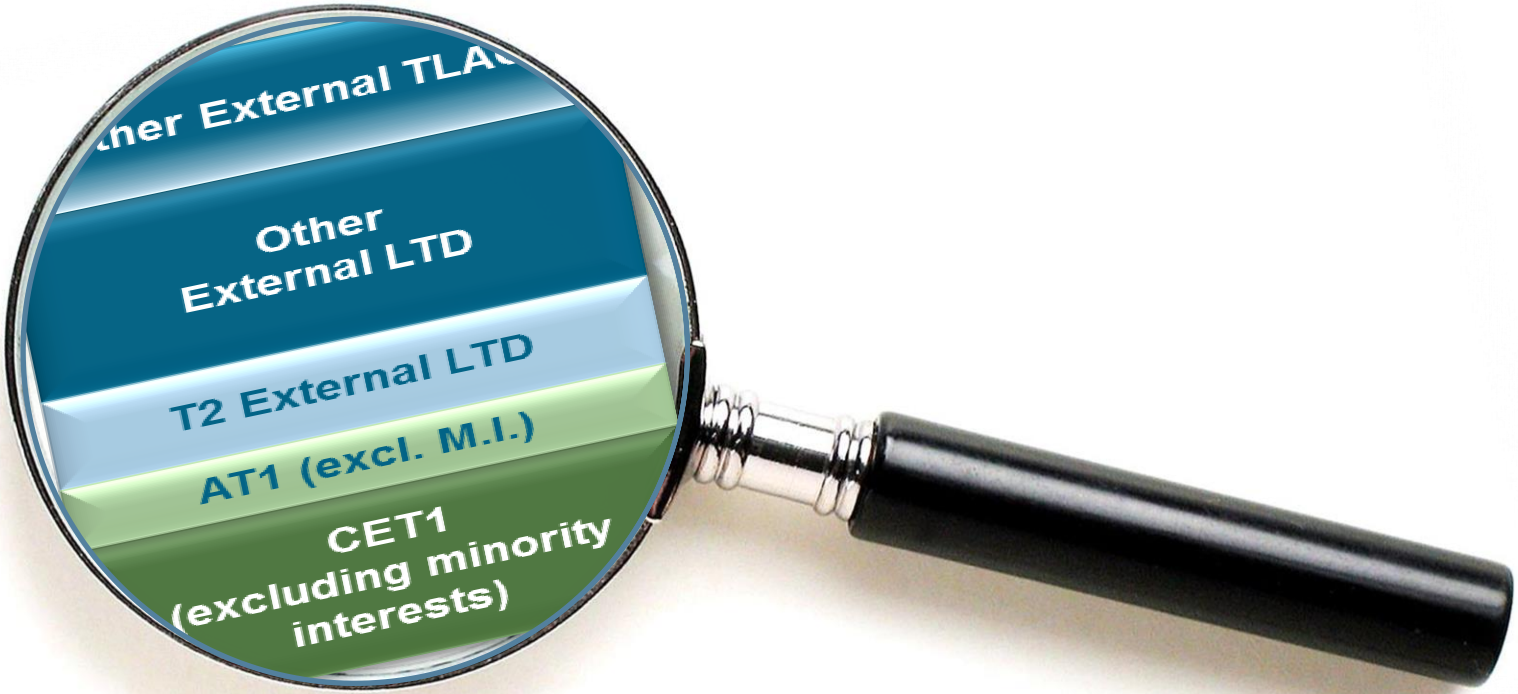
Federal Reserve’s Proposed Rule on Total Loss-Absorbing Capacity and Eligible Long-Term Debt



November 10, 2015

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Table of Contents

I. Introduction and Scope

Overview of Proposed Rule on TLAC and Eligible LTD

- The Federal Reserve has issued a proposed rule that is intended to further improve the resiliency and resolvability of certain U.S. banking organizations through new enhanced prudential standards that would impose:
  - **Total loss-absorbing capacity (TLAC)** requirements (i.e., combined eligible Tier 1 regulatory capital and eligible LTD);
  - Separate **eligible long-term debt (LTD)** requirements; and
  - Clean holding company requirements designed to make short-term unsecured debt (including deposits) and most other ineligible liabilities structurally senior to eligible LTD.
- These enhanced prudential standards would apply to:
  - Top-tier U.S. bank holding companies identified by the Federal Reserve as **global systemically important bank holding companies (G-SIB BHCs)**; and
  - U.S. **intermediate holding companies** of global systemically important foreign banking organizations with at least $50 billion in U.S. non-branch assets **(covered IHCs)**.
- The proposed rule would also require banking organizations subject to the Federal Reserve's Basel III capital rules to deduct from regulatory capital any investments in unsecured debt issued by G-SIB BHCs.
- The Federal Reserve estimates that its proposed rule would impose an aggregate eligible external LTD requirement on the G-SIB BHCs of $680 billion, compared to **at least** $590 billion* in existing LTD, for a shortfall of $90 billion in new eligible LTD.
  - The Federal Reserve's estimate assumes that existing external LTD will qualify as eligible LTD or be grandfathered, even though none of the outstanding external LTD would appear to qualify as eligible LTD and the proposed rule does not currently include a grandfathering provision.
- Most of the proposed requirements would be effective as of **January 1, 2019**, with a transition period to **January 1, 2022** for the risk-based ratio component of the proposed TLAC requirements.
- The comment period for the proposed rule ends on **February 1, 2016**.
- A copy of the proposed rule and Preamble is available here, and the Federal Reserve's staff memo is available here.

* The actual amount of existing LTD may be closer to $700 billion, since several G-SIB BHCs already have existing LTD substantially in excess of the required minimum, whereas other G-SIB BHCs account for the aggregate shortfall.

Which Organizations Are Affected?

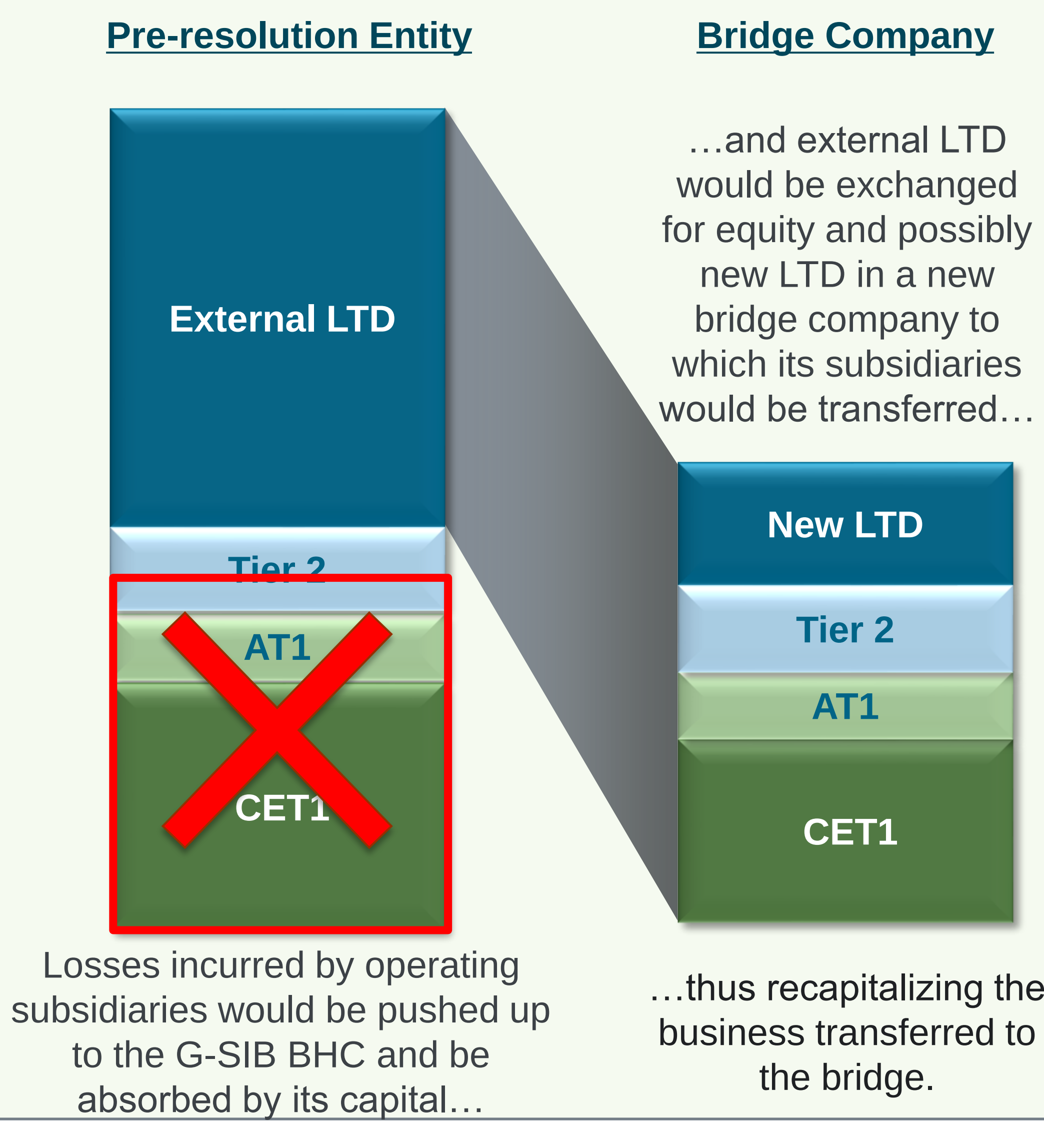
Proposed Requirement	Covered Institutions
Minimum external TLAC and external LTD, plus external TLAC buffer	▪ G-SIB BHCs ▪ Bank of America, Bank of New York Mellon, Citigroup, Goldman Sachs, JPMorgan Chase, Morgan Stanley, State Street and Wells Fargo
Minimum internal TLAC and internal LTD, plus internal TLAC buffer	▪ Covered IHCs ▪ U.S. IHCs of foreign G-SIBs, including Barclays, BNP Paribas, Deutsche Bank, Credit Suisse, HSBC, MUFG, Société Générale and UBS, and the IHCs of any other foreign G-SIBs identified pursuant to the methodology described on page 25.
Clean holding company restrictions	▪ G-SIB BHCs ▪ Covered IHCs
Capital deductions for investments in unsecured debt of G-SIB BHCs	**Applicability Under the Proposed Rule** ▪ State member banks ▪ BHCs and savings and loan holding companies (SLHCs) with ≥ $1 billion in total consolidated assets (except for SLHCs that are substantially engaged in insurance underwriting or commercial activities) ▪ U.S. IHCs of foreign banking organizations formed to comply with the Federal Reserve's enhanced prudential standards **Future Applicability to Other Institutions** ▪ The Federal Reserve intends to consult with the OCC and FDIC to apply the deduction requirement to all other insured depository institutions. ▪ The proposed rule would not impose the deduction requirement on, or apply it to unsecured debt issued by, nonbank SIFIs, but the Federal Reserve would determine its applicability with respect to nonbank SIFIs after finalizing the capital framework for nonbank SIFIs.

II. TLAC and LTD Requirements for G-SIB BHCs

External TLAC and Eligible LTD

External LTD Supports SPOE Resolution Strategy

- The centerpiece of the proposed rule for G-SIB BHCs is the external LTD requirement.
- The purpose of the external LTD requirement is to enhance the resiliency and resolvability of a G-SIB BHC.
- In a **single point-of-entry (SPOE)** resolution, only the top-tier BHC would enter into a resolution proceeding, allowing operating subsidiaries to be recapitalized by pushing losses up to the BHC, transferring the subsidiaries to a new debt-free bridge holding company and keeping the subsidiaries out of insolvency proceedings. See **Appendix A** for a step-by-step illustration of an SPOE resolution.
- The top-tier BHC must have a minimum amount of structurally subordinated long-term debt to absorb losses in the BHC's resolution without fostering runs on the short-term debt of its operating subsidiaries, which can destabilize the financial system if the runs spread to other institutions.



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External TLAC and Eligible LTD

External TLAC and LTD Requirements

- The proposed rule would require G-SIB BHCs to maintain minimum ratios of external TLAC and external LTD, plus an external TLAC buffer. See pages 10-15 for details on the minimum external TLAC and external LTD requirements.
- TLAC would include all instruments that would count towards Tier 1 capital, except minority interests. TLAC buffer consists of CET1 capital.
- Both requirements would include **eligible debt securities** with a remaining maturity of at least 1 year. For more information on which liabilities would count as eligible debt securities, see page 8.
- The external LTD requirement would apply a 50% haircut to the principal amount of eligible debt securities with a remaining maturity of more than 1 year but less than 2 years.
- A G-SIB BHC may not redeem or repurchase external LTD prior to maturity without the Federal Reserve's prior approval if doing so would cause the G-SIB BHC to fall below its external LTD requirement.

External TLAC

=

Eligible debt securities with a remaining maturity ≥ 1 year

+

AT1 (excluding minority interests)

+

CET1 (excluding minority interests)

External LTD

=

Eligible debt securities with a remaining maturity ≥ 2 years

+

Eligible debt securities with a remaining maturity ≥ 1 year and < 2 years

(Subject to 50% haircut)

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External TLAC and Eligible LTD

Eligible Debt Securities

Eligible debt securities would be debt instruments that:

- Are **paid in** and issued by the G-SIB BHC;
- Are **not secured**, are **not guaranteed** by the G-SIB BHC or any of its subsidiaries, and are **not** subject to other arrangements that legally or economically **enhance the seniority** of the instruments;
- Have a maturity of **greater than one year** from the date of issuance;
- Are governed by **U.S. state or federal law**; and
- Are **plain vanilla**, meaning that they:
  - Do **not** provide the holder with a **contractual right to accelerate** payment of principal or interest, **except** a right that is exercisable on one or more **specified dates** or in the **event of insolvency** or upon a **payment default**;
  - Do **not** have **a credit-sensitive feature** (e.g., interest rate step-ups or other resets based in whole or part on the G-SIB BHC's credit quality), except that they may have an interest rate that is adjusted periodically independent of the G-SIB BHC's credit quality, in relation to general market interest rates or similar adjustments (e.g., ordinary interest rate step-ups or step-downs not based on the G-SIB BHC's credit quality);
  - Are **not structured notes** (see page 9); and
  - Have **no contractual provision** that permits the instruments to be **converted** into or **exchanged** for equity of the G-SIB BHC (i.e., CoCos).

- Eligible debt securities would be required to be structurally subordinated to the group's short-term unsecured debt and certain other prohibited liabilities, but would **not** be required to be contractually subordinated to the G-SIB BHC's other obligations. The Federal Reserve requests comment, however, on whether eligible debt securities should be required to be contractually subordinated to a G-SIB BHC's other liabilities.
- Otherwise eligible debt securities that give the investor a **put right** exercisable on a date certain **1 year or more** after the date of issuance would qualify as eligible debt securities, but their maturity date would be deemed to be the first date on which the put right may be exercised for purposes of the remaining maturity requirements of the proposed rule.
- The Federal Reserve requests comment on whether to remove any of the requirements from the definition of eligible debt securities, including the U.S. governing law requirement, as well as restrictions on structured notes, upstream guarantees and CoCos.

External TLAC and Eligible LTD

Structured Notes

The proposed rule would define a **structured note** as a debt instrument that:

- Has a principal amount, redemption amount, or stated maturity that is subject to reduction based on the performance of any asset, entity, index, or embedded derivative or similar embedded feature;
- Has an embedded derivative or similar embedded feature that is linked to one or more equity securities, commodities, assets, or entities;
- Does not specify a minimum principal amount due upon acceleration or early termination; **or**
- Is not classified as debt under GAAP.

The Federal Reserve stated in the Preamble to the proposed rule that the proposed definition of structured note is **not** intended to include otherwise eligible instruments that also:

- Are **non-dollar denominated**; or
- Have interest payments that are **linked to an interest rate index** (such as a floating rate note linked to the federal funds rate or to LIBOR).

Under the proposed rule, structured notes would not qualify as eligible LTD, even if they have an original maturity of more than one year and specify a minimum principal amount payable upon acceleration or early termination (i.e., they are principal protected).

Required External TLAC and External LTD Ratios

- G-SIB BHCs would be required to maintain minimum ratios of **external TLAC** and **external LTD**, each as a percentage of both risk-weighted assets (risk-based ratio requirements) and total leverage exposure (supplementary leverage ratio, or **SLR**, requirements).
- In addition, G-SIB BHCs would be required to maintain an **external TLAC buffer**, composed solely of CET1,* on top of the minimum external TLAC risk-based ratio, in order to avoid restrictions on distributions and discretionary bonus payments.

Minimum Ratio or Buffer	Proposed Risk-based Ratio Requirements		Proposed SLR Requirements
	Components of Requirement	Current Range**	
Minimum External TLAC Ratio	18% (on a fully phased-in basis)		9.5%
External TLAC Buffer	2.5% + Method 1 G-SIB surcharge + countercyclical buffer	3.5% to 5%	N/A
Minimum-plus-Buffer External TLAC Ratio	Minimum external TLAC + external TLAC buffer	21.5% to 23%	N/A
Minimum External LTD Ratio	6% + Method 2 G-SIB surcharge	7% to 10.5%	4.5%

The denominator in the risk-based ratio requirements is ***risk-weighted assets*** (RWAs). RWAs would be calculated using the same methodology for calculating the G-SIB BHC's RWAs under the existing U.S. Basel III capital rules.

The denominator used in the SLR requirements is ***total leverage exposure.*** Total leverage exposure, which is defined by the Federal Reserve's SLR rule, includes both on-balance sheet assets and off-balance sheet exposures such as those related to OTC derivatives, cleared derivatives, and repo-style transactions.

* As explained in **Appendix B**, the requirement that the external TLAC buffer be composed solely of CET1 is redundant in view of existing capital buffer requirements.

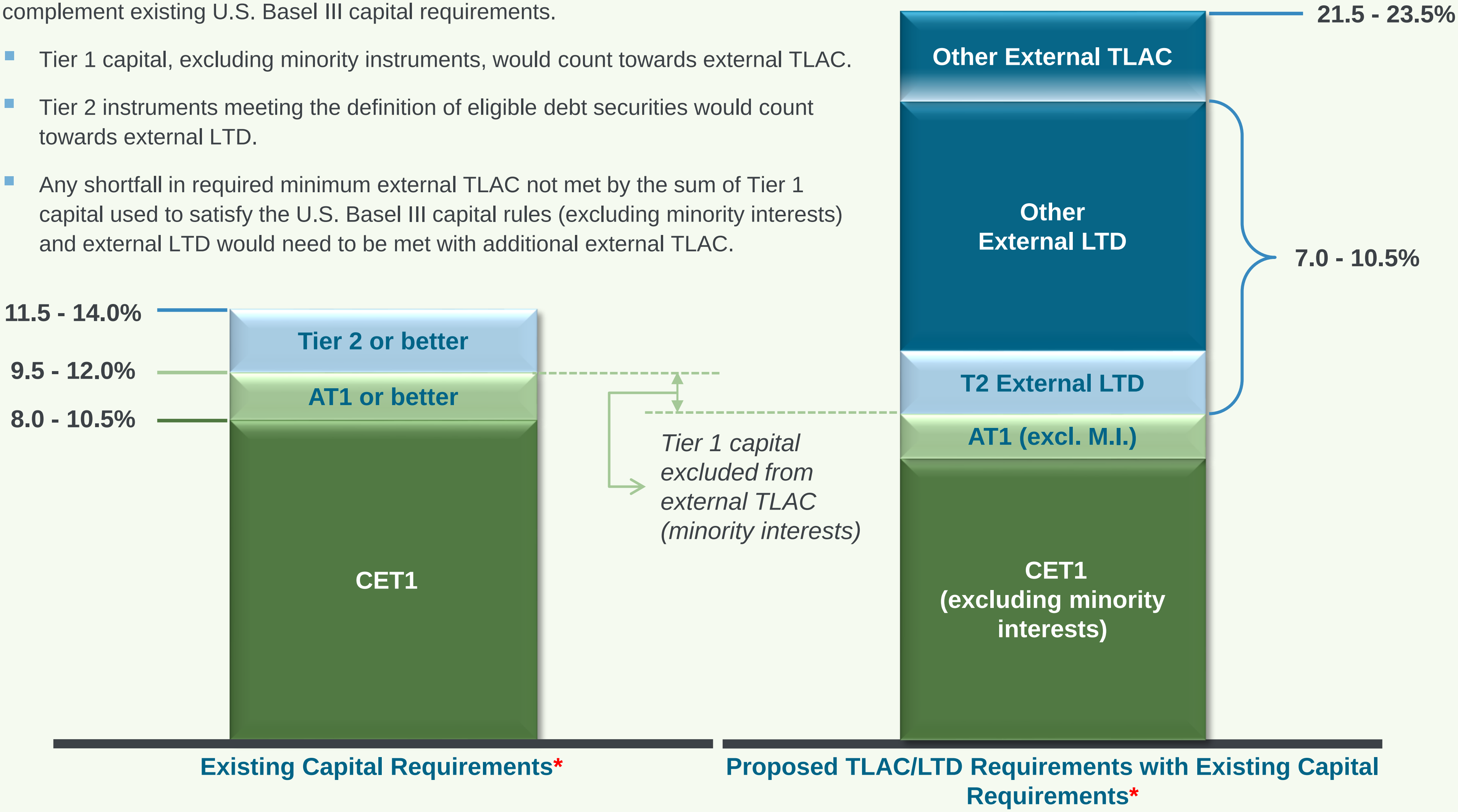
** The ***current range*** of the risk-based ratio requirements reflects the currently effective range of G-SIB surcharges for the eight G-SIB BHCs, based on estimates published by the Federal Reserve. Under the Federal Reserve's ***G-SIB surcharge*** final rule, the surcharge for each G-SIB BHC is equal to the greater of the surcharge as determined under two methods: **Method 1** and **Method 2**. Typically, **Method 2** will result in a higher surcharge. For G-SIB BHCs, Method 2 surcharges currently range between 1.0% and 4.5%, while Method 1 surcharges currently range between 1.0% and 2.5%.

Required External TLAC and External LTD Ratios

Risk-based Ratios and Their Relationship with Existing Capital Requirements

The proposed risk-based external TLAC and external LTD requirements would complement existing U.S. Basel III capital requirements.

- Tier 1 capital, excluding minority instruments, would count towards external TLAC.
- Tier 2 instruments meeting the definition of eligible debt securities would count towards external LTD.
- Any shortfall in required minimum external TLAC not met by the sum of Tier 1 capital used to satisfy the U.S. Basel III capital rules (excluding minority interests) and external LTD would need to be met with additional external TLAC.



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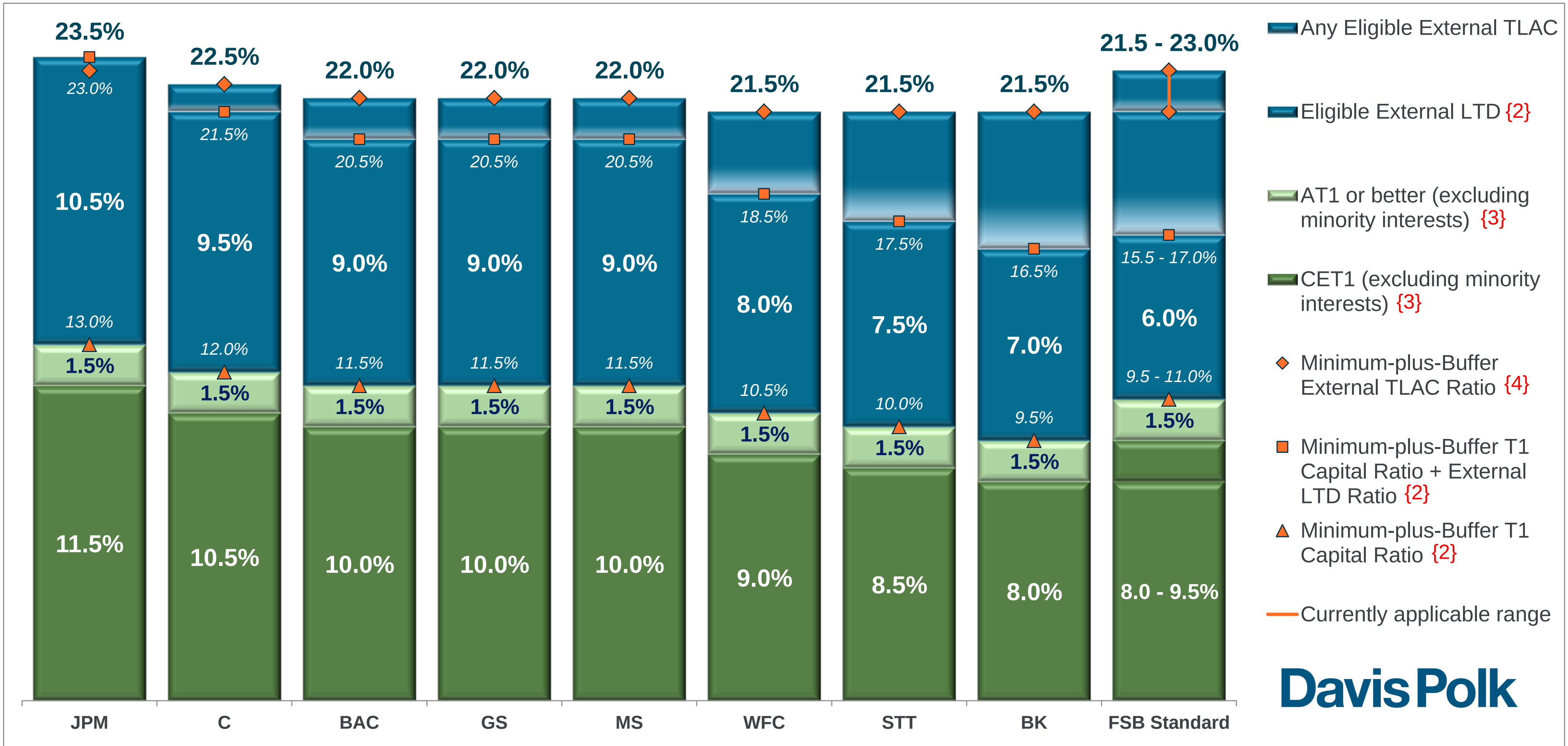
* On a fully phased-in basis, including capital conservation buffers and G-SIB surcharges, and assuming no countercyclical buffer is in effect.

Required External TLAC and External LTD Ratios

Estimated Fully Phased-In Risk-based Requirements by G-SIB BHC[1]



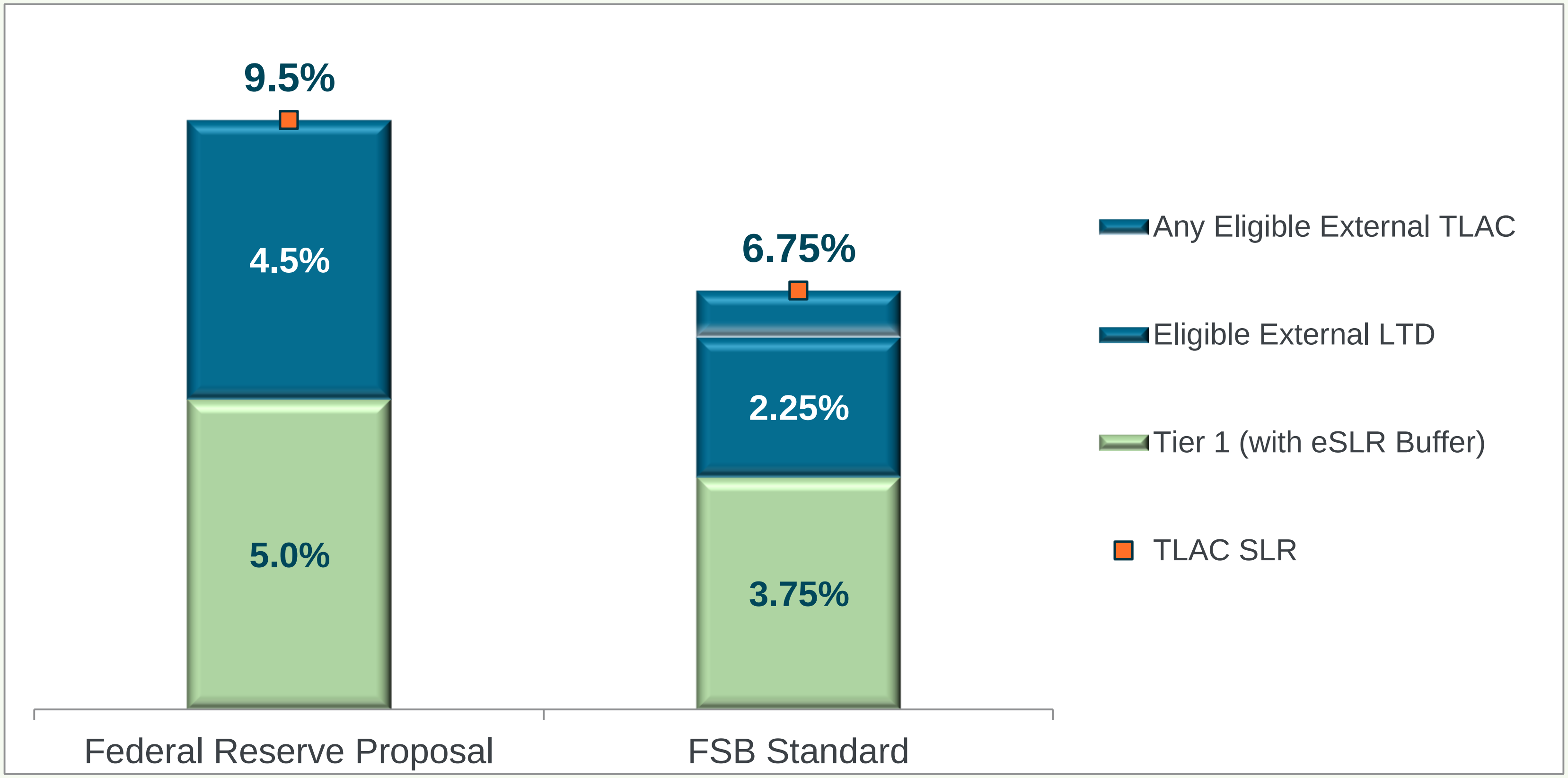
[1] This chart does not depict any higher amount of external LTD or external TLAC that could be required under the proposed external LTD SLR and external TLAC SLR requirements. Nor does it reflect capital that would be needed to maintain applicable minimum requirements on a stressed basis.

[2] Includes each firm's method 2 G-SIB surcharge--which is applied to the minimum external LTD risk-based ratio and the CET1 capital buffers--based on Federal Reserve estimates disclosed with the G-SIB surcharge final rule in July 2015.

[3] Although minority interests are excluded from eligible TLAC, we have not adjusted minimum capital ratios and capital buffers to correct for the fact that these amounts are not similarly excluded from capital. Thus, we assume for purposes of this chart that minority interests recognized in T1 capital are de minimis.

[4] Includes each firm's method 1 G-SIB surcharge--which is applied to the minimum-plus-buffer external TLAC risk-based ratio--based on FR Y-15 disclosures as of YE 2014.

Required External TLAC and External LTD Ratios
SLR Requirements



External TLAC Buffer Requirement

- The proposed rule introduces an **external TLAC buffer**, which would be required to be composed solely of CET1.*

External TLAC Buffer Requirement = 2.5% + Method 1 G-SIB Surcharge + Countercyclical Buffer

- The TLAC buffer would impose a TLAC buffer above the external TLAC risk-based requirement and would operate in the same way as the capital conservation buffer and G-SIB surcharge under the U.S. Basel III capital rules.**
- The buffer would be required to be maintained to avoid:
  - Limitations on capital distributions (e.g., repurchases of capital instruments or dividend or interest payments on capital instruments); and
  - Limitations on discretionary bonus payments to executive officers such as the CEO, president, CFO, CIO, CLO and heads of major lines of business.
- As a banking organization dips further below the full required amount of its external TLAC buffer, it would be subject to increasingly stringent limitations on capital distributions and bonus payments:

Ratio of External TLAC Buffer Level to Requirement	Maximum Payout Ratio (as a % of eligible retained income)
> 100%	No payout limitation applies
> 75% and ≤ 100%	60%
> 50% and ≤ 75%	40%
> 25% and ≤ 50%	20%
≤ 25%	No capital distributions or discretionary bonus payments allowed

The payout limitation schedule would be identical to the limitation schedule for breaches of the capital buffers under the U.S. Basel III capital rules.

* As shown in **Appendix B**, the requirement that the external TLAC buffer be composed solely of CET1 is redundant in view of the capital buffer requirement.

** The Federal Reserve has requested comment on whether to calibrate the proposed external TLAC SLR requirement at 7.5% (instead of 9.5%) plus a buffer of 2% of total leverage exposure.

External TLAC Buffer Requirement
Calculation of External TLAC Buffer Level

- Each firm's **external TLAC buffer level** would be based on its risk-based capital and external LTD ratios, relative to the minimum required external TLAC risk-based ratio. It would be calculated using the following formula*:

External TLAC Buffer Level = **CET1 risk-based ratio *minus the greater of:***
- **zero *and***
- **[18% – AT1 (less tier 1 minority interests) risk-based ratio – external LTD risk-based ratio]**

- The formula would effectively prevent CET1 capital used to meet the minimum required external TLAC risk-based ratio from being included in the external TLAC buffer.

- Step 1: The formula first subtracts the amounts of the firm's AT1 (less Tier 1 minority interests) and external LTD from the applicable minimum requirement, each as a percentage of RWAs:

18% — **AT1** — **LTD** = ***Remainder of minimum required external TLAC to be met with CET1***

- Step 2: If a firm has enough AT1 (less Tier 1 minority interests) and external LTD to meet the minimum required external TLAC risk-based ratio without any CET1, then the external TLAC buffer level equals the firm's full amount of CET1:

External TLAC Buffer Level = **CET1**

- **Step 3:** Otherwise, the external TLAC buffer level equals the amount of the firm's CET1 remaining after applying CET1 toward the remainder from Step 1:

External TLAC Buffer Level = **CET1** — **18%** — **AT1** — **LTD**

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* Formula presented on a fully phased-in basis. Please see **Appendix B** for a hypothetical set of calculations.

Clean Holding Company Framework

The proposed rule would establish a **clean holding company** framework that imposes certain restrictions on the types of liabilities that may be held at the level of the G-SIB BHC.

Prohibited Liabilities

- A G-SIB BHC would be prohibited from issuing short-term debt, creating setoff rights against subsidiaries, entering QFCs with third parties, issuing guarantees with certain prohibited cross-defaults or benefiting from upstream guarantees. For more details, see page 17.

5% Capped Liabilities

- There would be a 5% cap on the aggregate amount of certain non-contingent liabilities owed to third parties. For more details, see page 18.

Permissible Ineligible Liabilities

- Certain liabilities that would not qualify as eligible external LTD would be permitted to remain *pari passu* or junior to eligible external LTD.
- Includes all liabilities that fall outside the definitions of eligible LTD, prohibited liabilities and capped liabilities.
- These liabilities would not count toward the 5% cap.

The proposed rule text indicates that most of the prohibitions apply **prospectively** only to instruments or contracts issued or entered into on or **after January 1, 2019**.

This framework is designed to make short-term debt (including deposits) and most other ineligible liabilities structurally senior to eligible external LTD, so that losses may be imposed on eligible external LTD without imposing them pro rata on short-term unsecured debt and most other ineligible unsecured liabilities. The primary purpose of this creditor hierarchy is to reduce the risk of runs by the holders of short-term debt (including deposits) and the sort of contagion that can destabilize the U.S. financial system.

Please refer to page 19 for a table providing a non-exclusive list of expected prohibited, capped and permissible liabilities.

Clean Holding Company Framework

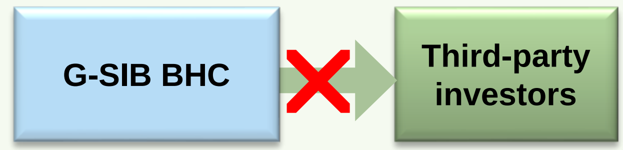
Prohibited Liabilities

A G-SIB BHC may **not**:

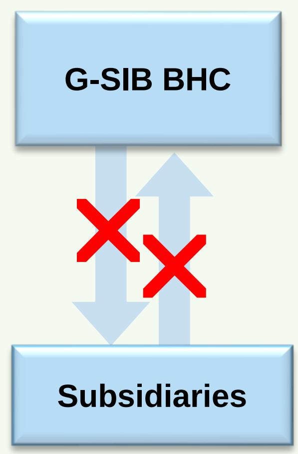
- **Issue** any **short-term debt instrument** (i.e., an instrument with an original maturity of less than one year, such as commercial paper), including short-term deposits and demand deposits,* to any person other than a subsidiary of the G-SIB BHC;
- **Issue** any instrument, or enter into any related contract, with respect to which the holder of the instrument has a **contractual right to offset** debt owed to a subsidiary of the G-SIB BHC by the holder or its affiliates **against the amount owed by the G-SIB BHC** under the instrument;
- **Enter** into a **qualified financial contract (QFC)** with a person that is not a subsidiary of the G-SIB BHC;
- **Guarantee** a liability of a subsidiary of the G-SIB BHC if such liability permits the exercise of a **cross-default right** that is related, directly or indirectly, to the **G-SIB BHC's insolvency** or similar proceeding, except for a resolution proceeding under Title II of the Dodd-Frank Act; or
  - The Preamble indicates that parent guarantees of QFCs engaged in by a subsidiary of a G-SIB BHC adhering to the ISDA Protocol should be permissible.
- **Enter into**, or otherwise benefit from, any agreement that provides for its liabilities to be guaranteed by any of its subsidiaries (**upstream guarantees**).

These prohibitions apply whether or not the liabilities are secured or made senior to eligible LTD by statute or contract.

This requirement appears to prohibit a G-SIB BHC or a bridge financial company that succeeds to the G-SIB BHC's business from obtaining secured liquidity from the private or public sector, including from the orderly liquidation fund (OLF) in a resolution proceeding under Title II of Dodd-Frank or from a debtor-in-possession (DIP) facility in a bankruptcy proceeding.



- **Short-term debt**
- **Cross-affiliate netting**
- **QFCs**



- **Guarantees with impermissible cross-default rights**
- **Upstream guarantees**

* U.S. law already prohibits BHCs from taking deposits.

Clean Holding Company Framework
Capped Liabilities

The proposed rule would impose a cap on the aggregate amount, measured on an **unconsolidated** basis, of certain unrelated liabilities equal to 5% of the particular G-SIB BHC's external TLAC.

$$\frac{\textbf{Unrelated Liabilities}}{\textbf{External TLAC}} \leq \textbf{5\% Cap}$$

Unrelated liabilities would include any **non-contingent** liability of the G-SIB BHC owed to a person that is **not an affiliate** of the G-SIB BHC, **other than**:

- Eligible external TLAC;
- Any dividend or other liability arising from eligible external TLAC;
- An instrument that was once an eligible debt security that does not provide the holder of the instrument with a currently exercisable right to require immediate payment of the total or remaining principal amount (e.g., a previously eligible debt security that has a remaining maturity of less than one year); or
- A secured liability, to the extent that it is secured, or a liability that otherwise represents a claim that would be senior to eligible debt securities under Title II of the Dodd-Frank Act or the Bankruptcy Code.

The G-SIB BHC's actual **Tier 1 Capital** (excluding any Tier 1 minority interests) **+ Eligible Debt Securities**

Clean Holding Company Framework

Examples of Prohibited, Capped and Permissible Liabilities

Prohibited Liabilities

- Any short-term debt instrument issued to a third party, including:
  - Commercial paper
  - Short-term deposits*
  - Demand deposits*
- Instruments with a contractual right to offset debt owed to a subsidiary by the holder against the amount owed by the G-SIB BHC
- QFCs with a third party
- Guarantees of a subsidiary liability with cross-default rights related to the G-SIB BHC's insolvency
- Upstream guarantees

These liabilities are all prohibited even if they are secured or otherwise made senior to eligible LTD by statute or contract.

Capped Liabilities

- Legacy and new LTD that has acceleration rights for defaults other than insolvency or payment defaults
- Structured notes, including principal protected long-term structured notes
- Plain vanilla LTD governed by non-U.S. law
- External vendor and operating liabilities that are non-contingent, including non-contingent liabilities for:
  - Utilities and rent
  - Fees for services
  - Obligations to employees
- Liabilities arising other than through a contract, if non-contingent, including:
  - Liabilities created by a court judgment
- CoCos

In each case, unless permitted or grandfathered in the final rule, or unless secured or otherwise made senior to eligible LTD.

Permissible Ineligible Liabilities

- Liabilities to a subsidiary, including short-term debt and QFC liabilities, whether secured or unsecured
- Debt instruments that otherwise qualify as eligible TLAC except that they have a remaining maturity of less than a year, as long as the holder does not have a currently exercisable put right
- Payables (such as dividends or interest-related payables) associated with eligible TLAC
- Liabilities that are secured or senior to eligible debt securities by statute or contract that are not prohibited liabilities, such as certain federal tax liabilities
- Contingent liabilities that are not otherwise prohibited liabilities, including:
  - BHC's guarantees of subsidiary liabilities
  - Obligations under executory contracts that are not yet payable (e.g., for future rent periods on a long-term lease)

* U.S. law already prohibits BHCs from taking deposits.

No Grandfathering of Legacy LTD

- The proposed rule does **not** include grandfathering for legacy LTD, including LTD issued between the dates of the proposed and final rule.
  - The Federal Reserve requests comment on whether grandfathering for certain existing liabilities that would be subject to the 5% cap, including legacy structured notes and other ineligible legacy LTD, would be appropriate, and indicates that any such request should include data illustrating the scope of the problem and seriousness of impediments to conformance.
- It is **unclear** whether legacy LTD, including LTD issued between the dates of the proposed and final rule, with certain standard features, such as acceleration rights for breaches of certain covenants, will ultimately be grandfathered or whether they will be treated as eligible debt securities, permissible ineligible liabilities or capped liabilities.
  - The Federal Reserve expressly permitted acceleration rights for payment defaults on the basis that these rights are a standard feature of existing senior debt securities and out of a desire not to be unduly disruptive of the market.
    - Acceleration rights for breaches of certain other covenants are **also a standard feature** of existing, and likely many interim, senior debt securities.
    - The Federal Reserve's estimates of how much new LTD will be required for G-SIB BHCs to comply with the new rule seem to assume that most if not all legacy LTD will qualify or be grandfathered in the final rule. See page 3.
  - The Federal Reserve, however, is also considering whether to impose a restriction on eligible LTD that is identical to the one applicable to Tier 2 capital by also prohibiting eligible external LTD from containing payment default acceleration clauses.

The Federal Reserve's proposed rule sent conflicting signals on the treatment of legacy LTD, including LTD issued between the dates of the proposed and final rules. On the one hand, the Federal Reserve's estimate of the incremental amount of LTD that the G-SIB BHCs would have to raise to comply with the LTD proposal ($90 billion) assumed that legacy LTD (estimated by the Federal Reserve to be at least $590 billion and probably closer to $700 billion) would not need to be replaced. In addition, the Preamble states that the Federal Reserve tried to structure its proposed rule to avoid being unduly disruptive of the market for senior debt issued by the G-SIB BHCs. On the other hand, the text of the proposed rule defined eligible LTD in a way that would not currently include legacy LTD and did not include an express grandfathering provision for legacy LTD.

Disclosure Requirements

- G-SIB BHCs would be required to publicly disclose a description of the financial consequences to unsecured debtholders if the G-SIB BHC were to enter into a resolution proceeding in which it is the only entity subject to the proceeding.
  - This disclosure would be required to be included in the offering documents for all of the G-SIB BHC's new issuances of eligible debt securities.
  - The disclosure also would be required to be provided publicly in one of the following ways:
    - By posting the disclosure on the G-SIB BHC's public website, or
    - By including the disclosure in more than one public financial report or other public regulatory report, provided that the G-SIB BHC publicly provides a summary table specifically indicating the location of the disclosure.
- It is likely that the market will expect disclosure well in advance of the final rule.
- The Federal Reserve stated that it plans to propose for comment a requirement that G-SIB BHCs and covered IHCs publicly report, on a regular basis, the amounts of their eligible external TLAC and LTD and eligible internal TLAC and LTD.

Consideration of Domestic Internal TLAC Requirement

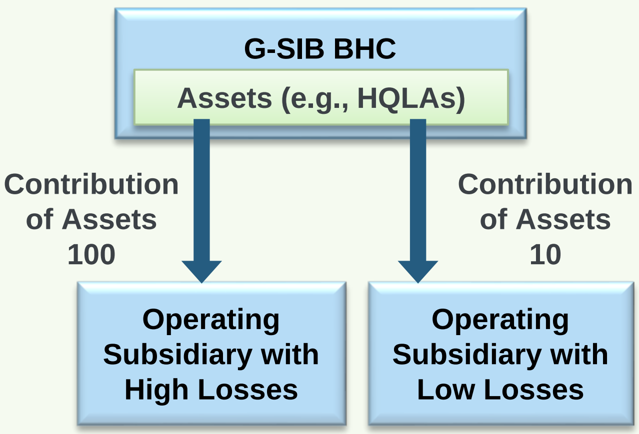
- The proposed rule does not include a domestic internal TLAC requirement, but the Federal Reserve stated that it is considering including such a framework divided into two categories: **Contributable Resources** and **Prepositioned Resources**.*

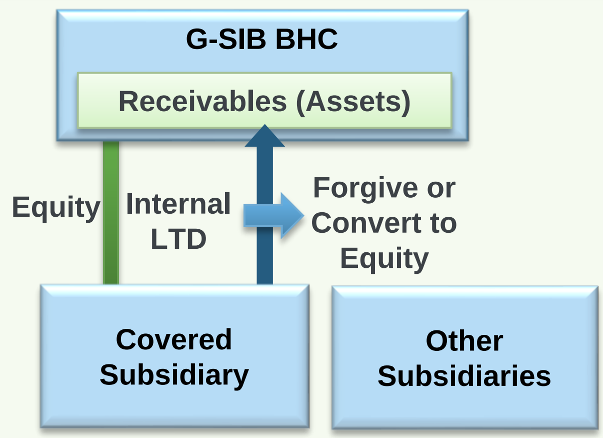
Contributable Resources

- The G-SIB BHC might be required to hold a certain amount of assets, possibly limited to **high-quality liquid assets (HQLAs)** at the parent company.
- These assets could be allocated flexibly among subsidiaries in light of the losses they suffer.

Prepositioned Resources

- The G-SIB BHC might be required to pre-position internal TLAC at certain **covered subsidiaries**.
- Upon the occurrence of specific trigger(s), any internal LTD might be forgiven or converted to equity.
- The Federal Reserve might require the debt to be unsecured, plain vanilla, have a remaining maturity of >1 year, and be contractually subordinated to third-party claims.
- The Federal Reserve is seeking comment on which subsidiaries should be covered subsidiaries that might be subject to a prepositioning requirement.





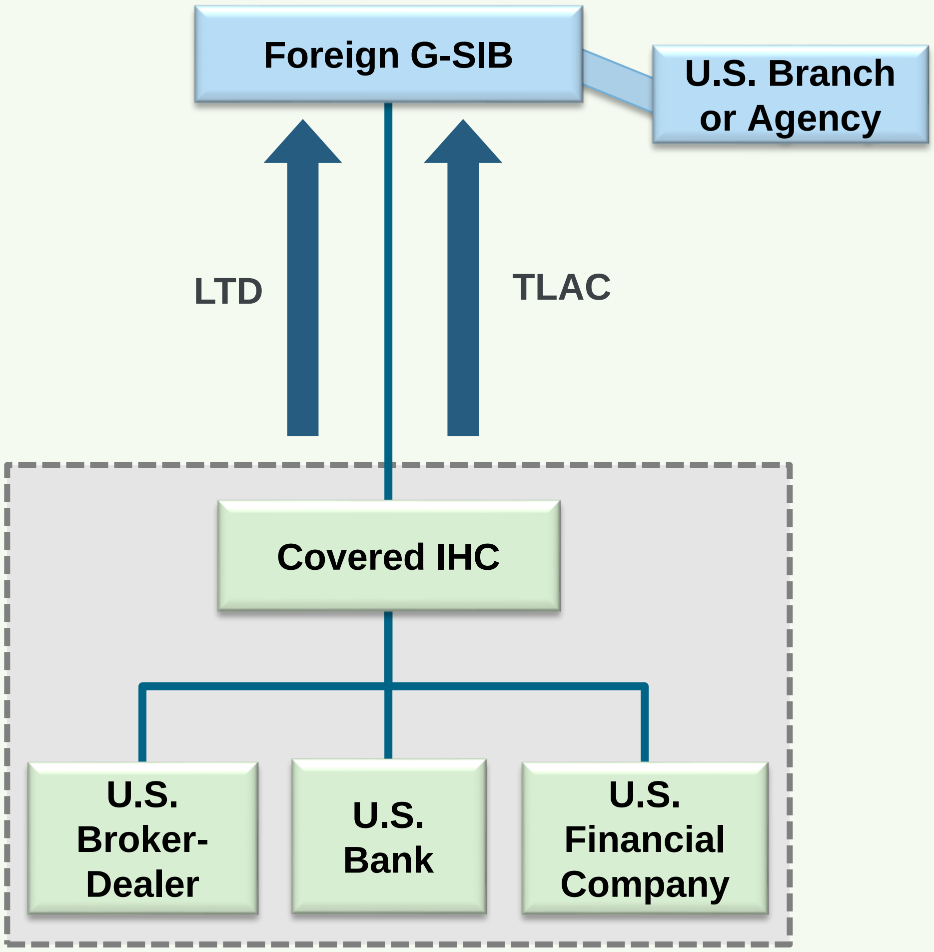
The distinction between contributable and prepositioned resources is somewhat artificial since a G-SIB BHC's receivables based on a subsidiary's internal LTD are assets of the G-SIB BHC and therefore contributable resources to another subsidiary, unless the Federal Reserve or the FDIC prohibits the G-SIB BHC from using its intercompany receivables (assets) in this manner.

* The Federal Reserve requested comment on a variety of issues, including whether contributable resources or prepositioned resources should be subject to capital contribution agreements that require the G-SIB BHC to use such resources to recapitalize specified subsidiaries upon specified trigger events.

III. Internal TLAC and LTD Requirements for Covered IHCs

Internal TLAC and Eligible LTD

- The proposed rule would amend the Federal Reserve's enhanced prudential standards applicable to **foreign banking organizations (FBOs)** to impose internal TLAC, internal LTD and clean holding company requirements on covered IHCs, i.e., all U.S. IHCs that are required to be formed under the enhanced prudential standards **and** that are controlled by a global systemically important FBO (foreign G-SIB).
- A key difference compared to the requirements for G-SIB BHCs is that, for instruments to count as internal TLAC or internal LTD, they must be **issued to a foreign parent entity** of the covered IHC (among other conditions) instead of to an unaffiliated third party.
    - This requirement is designed to ensure that losses incurred by the covered IHC can be pushed up to a foreign parent by the Federal Reserve.



Internal TLAC and Eligible LTD

Scope of Covered IHCs

- **Determination of Foreign G-SIB Status:** Under the proposed rule, a **top-tier FBO* that controls a U.S. IHC (IHC parent)** would be a foreign G-SIB if:
  - The IHC parent determines that it has the characteristics of a foreign G-SIB under the assessment methodology and higher loss absorbency requirement for global systemically important banks issued by the Basel Committee on Banking Supervision (**BCBS methodology**); **or**
  - The Federal Reserve, using information reported by the IHC parent or its U.S. subsidiaries, publicly available information and confidential supervisory information, determines that:
    - The IHC parent would be a G-SIB under the BCBS methodology;
    - The IHC parent would be identified as a G-SIB BHC under the Federal Reserve's capital rules relating to G-SIB surcharges; **or**
    - The U.S. IHC itself would be identified as a G-SIB BHC under the Federal Reserve's capital rules relating to G-SIB surcharges.
- **Notice Regarding G-SIB Status:** Each IHC parent would be required to notify the Federal Reserve by January 1 of each year:
  - Whether its home country supervisor or other appropriate home country regulatory authority has adopted standards consistent with the BCBS methodology; **and**
  - Whether the IHC parent prepares or reports the indicators used by the BCBS methodology to identify a banking organization as a G-SIB and, if it does, whether the IHC parent has determined that it has the characteristics of a G-SIB under the BCBS methodology using such data.
- The notice requirement for IHC parents would be effective starting **January 1, 2017**.

* Under the proposed rule, a "top-tier foreign banking organization" would be a foreign bank with a commercial banking presence in the U.S. unless the foreign bank is directly or indirectly controlled by one or more other companies, in which case the top-tier FBO would be the top-tier entity that controls the foreign bank **or** a subsidiary of the top-tier entity if specified by the Federal Reserve.

Internal TLAC and Eligible LTD

Eligible Internal Debt Securities

While the definition of eligible internal debt securities tracks the definition of eligible external debt securities in certain respects, it also includes several additional or varying requirements.

- Eligible internal debt securities, similar to eligible external debt securities, are debt instruments that:
  - Are **paid in** and issued by the covered IHC;
  - Have a maturity of **greater than one year** from the date of issuance;
  - Are **plain vanilla** and are **not structured notes**; and
  - Are governed by **U.S. state or federal law**.
- The other requirements for eligible internal debt securities are the following:
  - **Issued to a foreign parent.** The debt securities must be issued to and remain held by **a** foreign parent entity of the covered IHC and cannot be issued to a U.S. affiliate or third parties.
    - This requirement would prevent the conversion of eligible internal TLAC into equity from effecting a change in control over the covered IHC.
  - **Contractual trigger.** The debt securities must include a contractual provision approved by the Federal Reserve that provides for the immediate conversion or exchange of the instrument into Common Equity Tier 1 of the covered IHC or the cancellation of the instrument, in either case upon the Federal Reserve's issuance of an internal debt conversion order, which can only be issued if certain strict conditions are satisfied (see page 28).

Note that eligible internal debt securities are **not** required to be issued to the top-tier FBO.

(continued on following page)

Internal TLAC and Eligible LTD

Eligible Internal Debt Securities *(cont.)*

(Continued from prior page)

- **Subordinated.** Eligible internal debt securities must be **unsecured** and represent the **most subordinated debt claim** in a resolution proceeding of the covered IHC.*
  - The Preamble says that the subordination requirement would **not** apply with respect to liabilities related to eligible internal TLAC (such as dividend- or interest-related payables associated with such liabilities).
- **Plain vanilla**. There are differences in the plain vanilla features required for eligible internal debt securities:
  - Eligible internal debt securities do **not** provide the holder with a **contractual right to acceleration** based on **any event** (not even on nonpayment or insolvency).
  - In contrast to eligible external debt securities, there is no requirement that eligible internal debt securities exclude instruments with a credit-sensitive feature.

Note that this standard is far stricter than the acceleration requirement for eligible external debt securities.

* The Preamble says that eligible internal LTD must be contractually subordinated to all third-party liabilities, but the text of the proposed definition just reads "subordinated," which suggests that subordination either by contract or statute would satisfy the rule text.

Internal TLAC and Eligible LTD

Internal Debt Conversion Order

- The contractual trigger requirement in internal eligible debt securities is intended to ensure that losses incurred by the covered IHC are pushed up to a foreign parent and the covered IHC does not have to enter into a resolution proceeding.
- The Federal Reserve would be permitted to issue an **internal debt conversion order**, activating the contractual trigger, if the following conditions are met:
  - The Federal Reserve has determined that the covered IHC is in **default or in danger of default**; **and**
  - **Any** of the following circumstances apply:
    - An FBO that directly or indirectly controls the covered IHC or any subsidiary of the IHC parent has been placed into resolution proceedings, including the application of statutory resolution powers, in its home country;
    - The home country supervisor of the IHC parent has consented or has not objected within 48 hours of notification by the Federal Reserve to the conversion, exchange or cancellation of the covered IHC's eligible internal debt securities; **or**
    - The Federal Reserve has made a written recommendation to the Secretary of the Treasury that the FDIC should be appointed as receiver of the covered IHC under Title II of the Dodd-Frank Act.

A covered IHC is in **default or in danger of default** if:

- A case has been, or likely will promptly be, commenced with respect to the covered IHC under the Bankruptcy Code;
- The covered IHC has incurred, or is likely to incur, losses that will deplete all or substantially all of its capital, and there is no reasonable prospect for the covered IHC to avoid such depletion;
- The covered IHC's assets are, or are likely to be, less than its obligations to creditors and others; **or**
- The covered IHC is, or is likely to be, unable to pay its obligations (other than those subject to a bona fide dispute) in the normal course of business.

Required Internal TLAC and Internal LTD Ratios

- **Internal TLAC and Internal LTD:** Covered IHCs would be required to maintain minimum ratios of internal TLAC and internal LTD, each as a percentage of RWAs (risk-based ratios), total leverage exposure (supplementary leverage ratios) and average total consolidated assets (U.S. Tier 1 leverage ratios).
  - A covered IHC would be prohibited from redeeming or repurchasing outstanding eligible internal LTD prior to maturity without the Federal Reserve's prior approval if the covered IHC would fall below its internal LTD requirement.
- **Internal TLAC Buffer**: Covered IHCs also would be required to maintain an internal TLAC buffer, composed solely of CET1, on top of the minimum internal TLAC risk-based ratio, in order to avoid restrictions on distributions and discretionary bonus payments.
  - Unlike the external TLAC buffer for G-SIB BHCs, the internal TLAC buffer would not include a G-SIB surcharge component (unless the covered IHC were itself a G-SIB BHC).

The Federal Reserve's proposed requirement that internal TLAC be issued to a foreign parent raises concerns over whether a foreign parent would be permitted to use its receivables (assets) on such internal TLAC to recapitalize a foreign sister company affiliate of the covered IHC. The proposed requirement could therefore have the effect of ring-fencing internal TLAC and related assets (including receivables on the internal TLAC), creating a new Federal Reserve-created obstacle to the orderly resolution of foreign G-SIBs under an SPOE resolution strategy.

If foreign authorities impose similar requirements on the material foreign subsidiaries of G-SIB BHCs, such requirements could become a new foreign regulator-imposed obstacle to the orderly resolution of a G-SIB BHC under SPOE.

Required Internal TLAC and Internal LTD Ratios

- **Resolution Entity vs. Non-Resolution Entity:** The minimum required internal TLAC and LTD ratios would differ depending on whether the covered IHC is a resolution entity or a non-resolution entity, with the latter subject to lower requirements.
  - A covered IHC is a non-resolution entity if the home country resolution authority for the IHC parent has certified to the Federal Reserve that the authority's planned resolution strategy for the IHC parent does not involve the covered IHC or the subsidiaries of the covered IHC entering resolution, receivership, insolvency or similar proceedings in the U.S., such as in a typical SPOE resolution.
  - A covered IHC would cease to be a non-resolution entity one year from the date the Federal Reserve first provides notice to the covered IHC that the home country resolution authority for the IHC parent has indicated that the authority's planned resolution strategy for the IHC parent involves the covered IHC or one or more of the subsidiaries of the covered IHC entering resolution, receivership, insolvency or similar proceedings in the U.S., such as in a multiple-point-of-entry (MPOE) resolution or certain hybrid SPOE/MPOE resolutions.

The Federal Reserve's proposed minimum internal TLAC risk-weighted ratio for IHCs that are non-resolution entities is 89% of the proposed minimum external TLAC risk-weighted ratio for G-SIB BHCs, which is at the high end of the 75-90% range for internal TLAC for material foreign subsidiaries established by the FSB in its final international TLAC standard.

If foreign countries follow the Federal Reserve's lead, foreign authorities may impose internal TLAC requirements on the material foreign subsidiaries of G-SIB BHCs at the high end of the range. This suggests a lack of trust among home and host supervisors in using contributable resources to recapitalize foreign subsidiaries.

Required Internal TLAC and Internal LTD Ratios

Minimum Ratio or Buffer	Resolution Entity IHCs (MPOE Strategy)			Non-Resolution Entity IHCs (SPOE Strategy)		
	Proposed Risk-Based Ratio Requirements	**Proposed SLR Requirements***	**Proposed U.S. Tier 1 Leverage Ratio Requirements**	**Proposed Risk-Based Ratio Requirements**	**Proposed SLR Requirements***	**Proposed U.S. Tier 1 Leverage Ratio Requirements**
Minimum Internal TLAC Ratio	18% (on a fully phased-in basis)	6.75%	9%	16% (on a fully phased-in basis)	6%	8%
Internal TLAC Buffer	2.5% + countercyclical buffer	N/A	N/A	2.5% + countercyclical buffer	N/A	N/A
Minimum-plus-Buffer Internal TLAC Ratio	Minimum internal TLAC + internal TLAC buffer	N/A	N/A	Minimum internal TLAC + internal TLAC buffer	N/A	N/A
Minimum Internal LTD Ratio	7%	3%	4%	7%	3%	4%

- The denominator in the risk-based ratio requirements is RWAs and would be calculated using the same methodology for calculating the covered IHC's RWAs under existing regulatory capital rules.
- The denominator used in the SLR requirements is total leverage exposure, which, as defined by the Federal Reserve's SLR rule, includes both on-balance sheet assets and off-balance sheet exposures such as those related to OTC derivatives, cleared derivatives and repo-style transactions.
- The denominator in the Tier 1 leverage ratio requirements is average total consolidated assets.

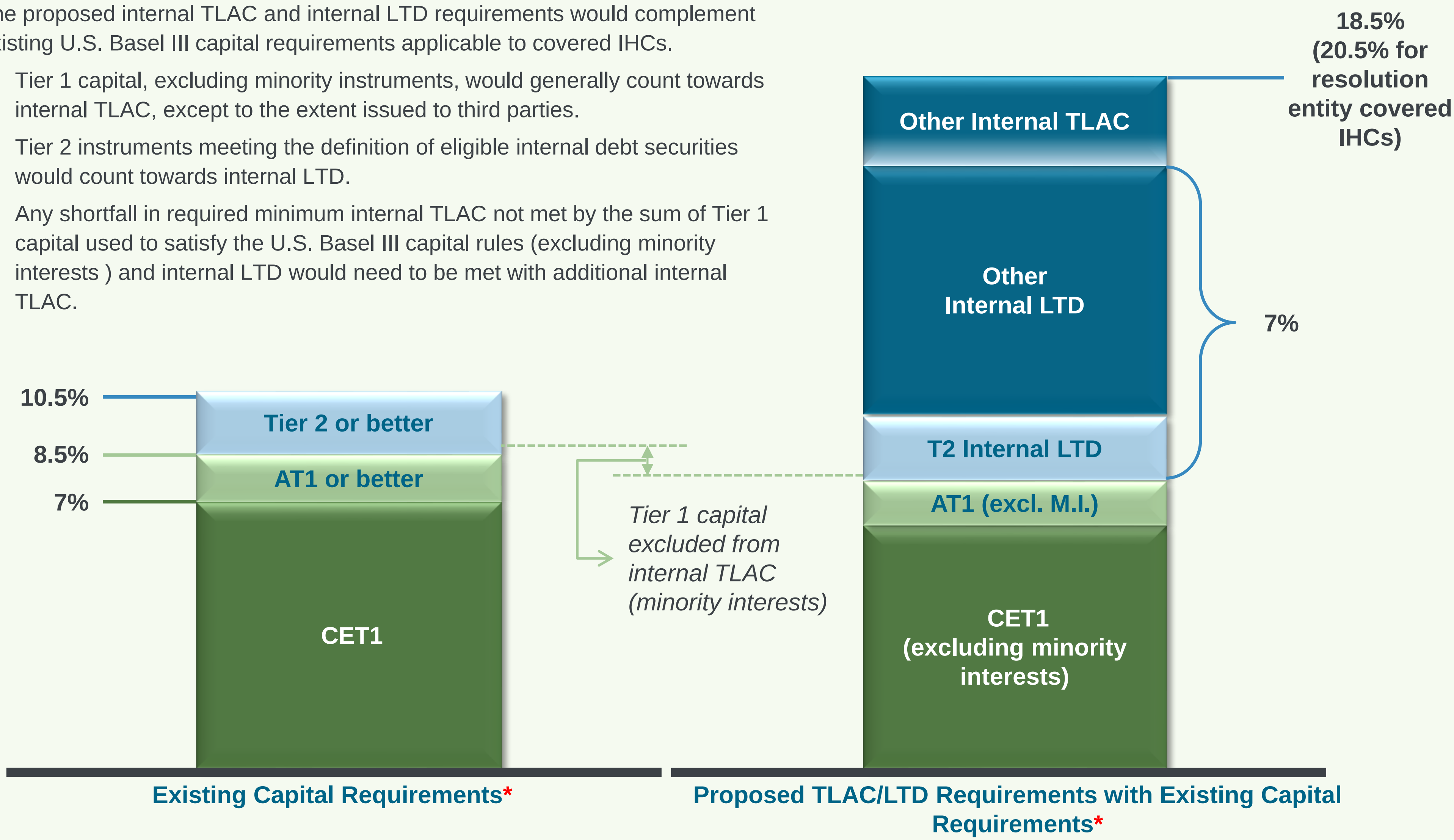
* Apply if the covered IHC has ≥ $250 billion of total consolidated assets or ≥ $10 billion of on-balance sheet foreign exposures.

Required Internal TLAC and Internal LTD Ratios

Risk-based Ratios and Their Relationship with Existing Capital Requirements

The proposed internal TLAC and internal LTD requirements would complement existing U.S. Basel III capital requirements applicable to covered IHCs.

- Tier 1 capital, excluding minority instruments, would generally count towards internal TLAC, except to the extent issued to third parties.
- Tier 2 instruments meeting the definition of eligible internal debt securities would count towards internal LTD.
- Any shortfall in required minimum internal TLAC not met by the sum of Tier 1 capital used to satisfy the U.S. Basel III capital rules (excluding minority interests) and internal LTD would need to be met with additional internal TLAC.



* On a fully phased-in basis, including capital conservation buffers and assuming no countercyclical buffer is in effect.

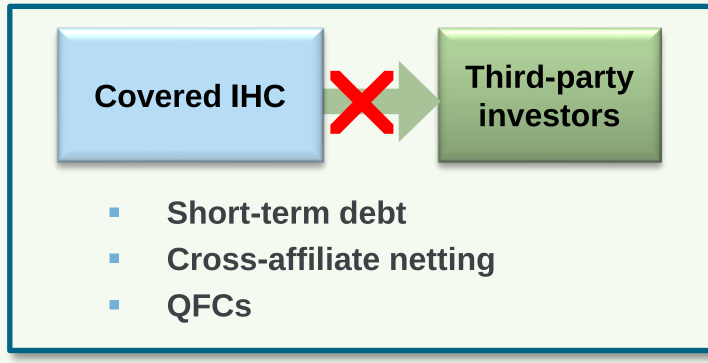
Clean Holding Company Framework

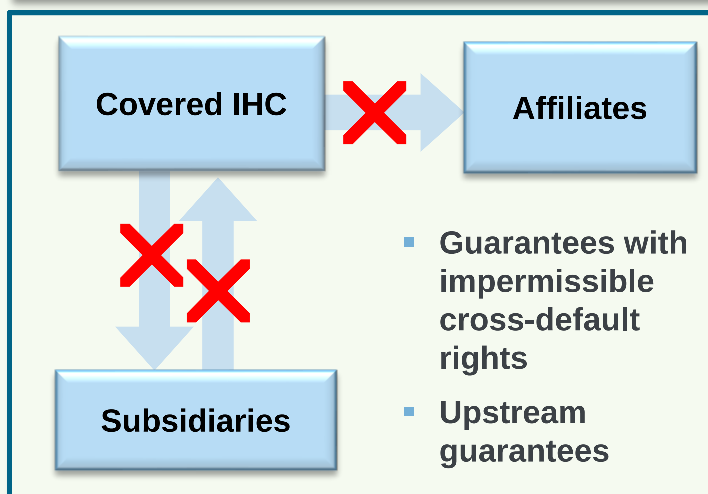
The clean holding company requirements for covered IHCs are similar to those for G-SIB BHCs, except that certain requirements apply with respect to affiliates instead of subsidiaries and there is no 5% cap on unrelated liabilities.

A covered IHC may **not**:

- Issue any short-term debt instrument (i.e., an instrument with an original maturity of less than one year), including short-term deposits and demand deposits,* to any person other than an affiliate of the covered IHC;
- Issue any instrument, or enter into any related contract, with respect to which the holder of the instrument has a contractual right to offset debt owed to the covered IHC or a subsidiary of the covered IHC by the holder or its affiliates against the amount owed by the covered IHC under the instrument;
- Enter into a QFC with a person that is not an affiliate of the covered IHC;
- Guarantee a liability of an affiliate of the covered IHC if such liability permits the exercise of a cross-default right that is related, directly or indirectly, to the covered IHC's insolvency or similar proceeding, except for a resolution proceeding under Title II of the Dodd-Frank Act; or
- Enter into, or otherwise benefit from, upstream guarantees.

This requirement appears to prohibit a covered IHC or a bridge financial company that succeeds to the IHC's business from obtaining secured short-term liquidity from the private or public sector, including from the OLF in a resolution proceeding under Title II of Dodd-Frank or from a DIP facility in a bankruptcy proceeding.





These prohibitions apply whether or not the liabilities are secured or made senior to eligible LTD by statute or contract.

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* U.S. law already prohibits covered IHCs from taking deposits.

IV. Capital Deduction for Investments in Unsecured Debt of G-SIB BHCs

Capital Deduction for Investments in Unsecured Debt of G-SIB BHCs

- The proposed rule would amend the U.S. Basel III capital rules applicable to **Board-regulated institutions** to require deductions from regulatory capital for certain investments in unsecured debt securities (whether or not eligible LTD) issued by G-SIB BHCs that do not qualify as Tier 2 capital (**covered debt instruments**).*
- These deductions would apply to **direct**, **indirect** (through investment funds) and **synthetic** exposures to covered debt instruments.
- The amount of the investment would be the Board-regulated institution's **net long position** in each covered debt instrument.

A **Board-regulated institution** is any:
- BHC or savings and loan holding company (SLHC), other than one subject to the Federal Reserve's Small Holding Company Policy Statement (generally, <$1 billion in total consolidated assets) and certain other categories of SLHCs;
- state member bank, or
- U.S. IHC.

Deduction Framework

- The proposed deduction for covered debt instruments would be implemented through the U.S. Basel III capital rules' existing deduction framework for **investments in unconsolidated financial institutions.**
- As under the existing U.S. Basel III capital rules, deductions for covered debt instruments as part of **non-significant investments** (i.e., 10% or less of the outstanding common stock) in G-SIB BHCs would generally be subject to the **10% threshold deduction approach**, whereby all investments subject to the approach are aggregated and subject to partial deduction—i.e., to the extent the aggregate amount exceeds a firm-specific threshold.
- Also consistent with the existing U.S. Basel III capital rules, certain categories of investments in covered debt instruments are not subject to the 10% threshold deduction approach and are instead subject to the **complete deduction approach**.
- All such deductions are made in accordance with the **corresponding deduction approach** (see page 36), with covered debt instruments treated as Tier 2 capital instruments.

Underwriting & Market-Making (consistent with the existing U.S. Basel III capital rules)

- Investments held as **underwriting positions** for five or fewer business days would be excluded from covered debt instruments.
- While the proposed rule would provide no specific market-making exception, the threshold deduction approach would generally apply to most market-making activity in covered debt instruments.

* Deductions are subject to a phase-in schedule.

Capital Deduction for Investments in Unsecured Debt of G-SIB BHCs *(cont.)*

Investments Subject to the Complete Deduction Approach

- If the Board-regulated institution is a G-SIB BHC, it would be required to deduct in **full**:
  - any investment in its **own covered debt instruments**.
  - any investment in a covered debt instrument that it is a **reciprocal cross holding** with another G-SIB BHC (i.e., held pursuant to a formal or informal agreement to swap, exchange or otherwise intend to hold each other's capital or covered debt instruments).
- If the Board-regulated institution holds a **significant investment** in any G-SIB BHC's common stock (i.e., >10% of the outstanding common stock of the G-SIB BHC), the Board-regulated institution would be required to deduct in **full** any investments in the capital or covered debt instruments of that G-SIB BHC not in the form of common stock, together with any such investments in other G-SIB BHCs.*

Non-Significant Investments Subject to the 10% Threshold Deduction Approach**

- Any of the Board-regulated institution's **non-significant investments** in covered debt instruments not otherwise subject to complete deduction would be subject to the 10% threshold deduction approach.
- As under the existing U.S. Basel III capital rules, the Board-regulated institution would be required to aggregate all non-significant investments in unconsolidated financial institutions (including G-SIB BHCs) and in the covered debt instruments of G-SIB BHCs, and deduct such aggregate amount to the extent it exceeds **10% of the Board-regulated institution's CET1 capital** (after applying certain regulatory adjustments and deductions).
- The Board-regulated institution would be required to **risk-weight** the portion of its investment in covered debt instruments not deducted using the otherwise applicable risk weights under the U.S. Basel III capital rules.

* Significant investments in common stock are subject to a separate threshold deduction approach not addressed in this memorandum.

** According to Federal Reserve analysis, Board-regulated institutions do not currently own substantial amounts of covered debt instruments.

Corresponding Deduction Approach (consistent with existing U.S. Basel III capital rules)

- Any deductions for investments in covered debt instruments would be subject to the corresponding deduction approach.
- Generally, under the corresponding deduction approach, investments in capital instruments are deducted from the capital category (e.g., CET1) corresponding to where the instrument is (or would be) categorized from the perspective of the issuer.
- Under the proposed rule, covered debt instruments would be treated as Tier 2 capital for purposes of the corresponding deduction approach.
- To the extent that the Board-regulated institution lacks sufficient Tier 2 capital from which to deduct its investment, the remaining amount would be sequentially deducted from each of the higher categories (i.e., first from Additional Tier 1 capital and then from CET1 capital).

Capital Deduction for Investments in Unsecured Debt of G-SIB BHCs *(cont.)*

Summary of Capital Deduction Framework for Investments in Covered Debt Instruments

- The following table summarizes the proposed treatment of investments in covered debt instruments under the proposed rule.

Category of Investment in Covered Debt Instrument	Type of Board-regulated Institution Holding the Investment	
	G-SIB BHC	Other Board-regulated Institution
Own Covered Debt Instrument	Complete Deduction Approach	N/A
Reciprocal Cross Holding	Complete Deduction Approach	N/A
Significant Investment*	Complete Deduction Approach	Complete Deduction Approach
Non-significant Investment*	10% Threshold Deduction Approach	10% Threshold Deduction Approach

Corresponding Deduction Approach (applicable to all deductions)

- The **amounts to be deducted** would be determined by application of either the complete deduction approach or the 10% threshold deduction approach, as applicable.
- The **location of the deduction** (i.e., which capital category against which to apply the deduction) would be determined by the **corresponding deduction approach.**
- For purposes of the corresponding deduction approach, covered debt instruments would be treated as **tier 2 capital instruments**.

*** Clarifying Note on "Significant Investments"**

- Whether an investment in a covered debt instrument would be treated as "significant" for purposes of the capital deduction framework would **not** turn on the absolute or relative size of the investment in the **covered debt instrument**.
- An investment in a covered debt instrument would be considered a "significant investment" if the Board-regulated institution also held a significant investment in the **common stock** of the issuing G-SIB BHC (i.e., >10% of the common stock outstanding).
- This use of the term "significant investment" is consistent with the terminology used in the existing U.S. Basel III capital rule, which treats investments in **non-common stock** capital instruments (e.g., Tier 2 instruments) of unconsolidated financial institutions as significant investments based on the proportion of the issuing institution's **common stock** held by the Board-regulated institution.

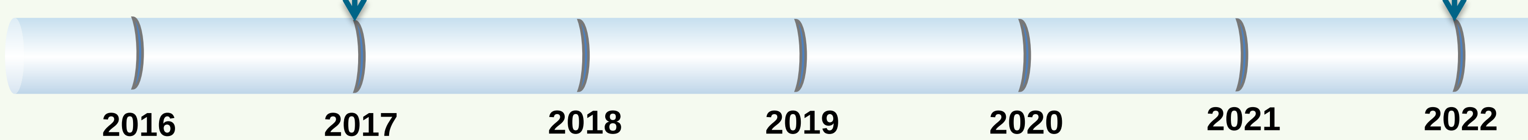
V. Compliance Timeline

Compliance Timeline

January 1, 2017
Notice requirements for parents of U.S. IHCs begin

January 1, 2022
The TLAC risk-based ratio increases to the fully phased-in level:

- 18% for G-SIB BHCs and covered IHCs that are resolution entities
- 16% for covered IHCs that are non-resolution entities



January 1, 2019
Compliance is required for all other elements of the rule, and the TLAC risk-based ratio is set at the transitional level:

- 16% for G-SIB BHCs and covered IHCs that are resolution entities
- 14% for covered IHCs that are non-resolution entities

Please refer to page 20 for more detail on the grandfathering of legacy LTD.

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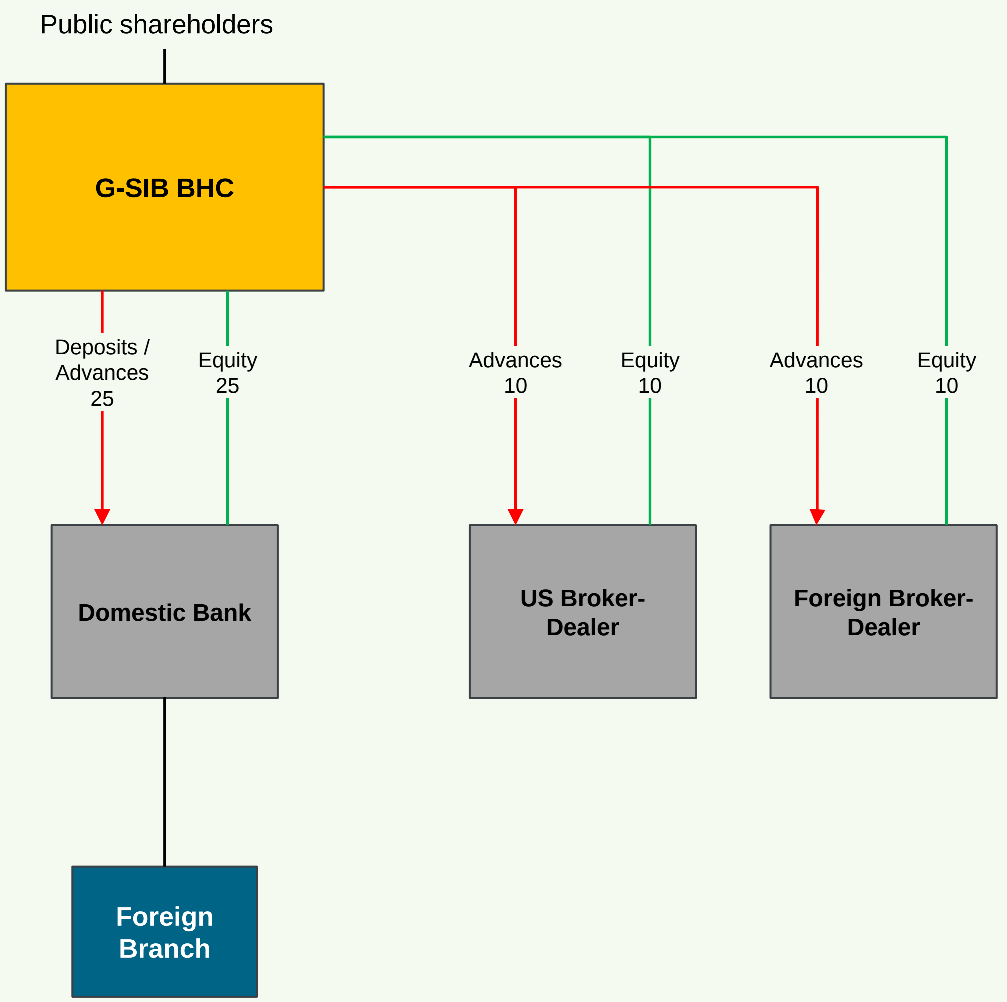
Appendix A: Step-by-Step Illustration of SPOE Resolution

Appendix A: Step-by-Step Illustration of SPOE Resolution

Group Structure Before Failure



Parent Only Balance Sheet

Deposits / advances to subs	45	Unsecured long-term debt	50
Equity in subs	45	Unsecured short-term debt	0
Other assets	10	Secured liabilities	0
Total	**100**	Other liabilities	5
		Equity	45
		Total	**100**

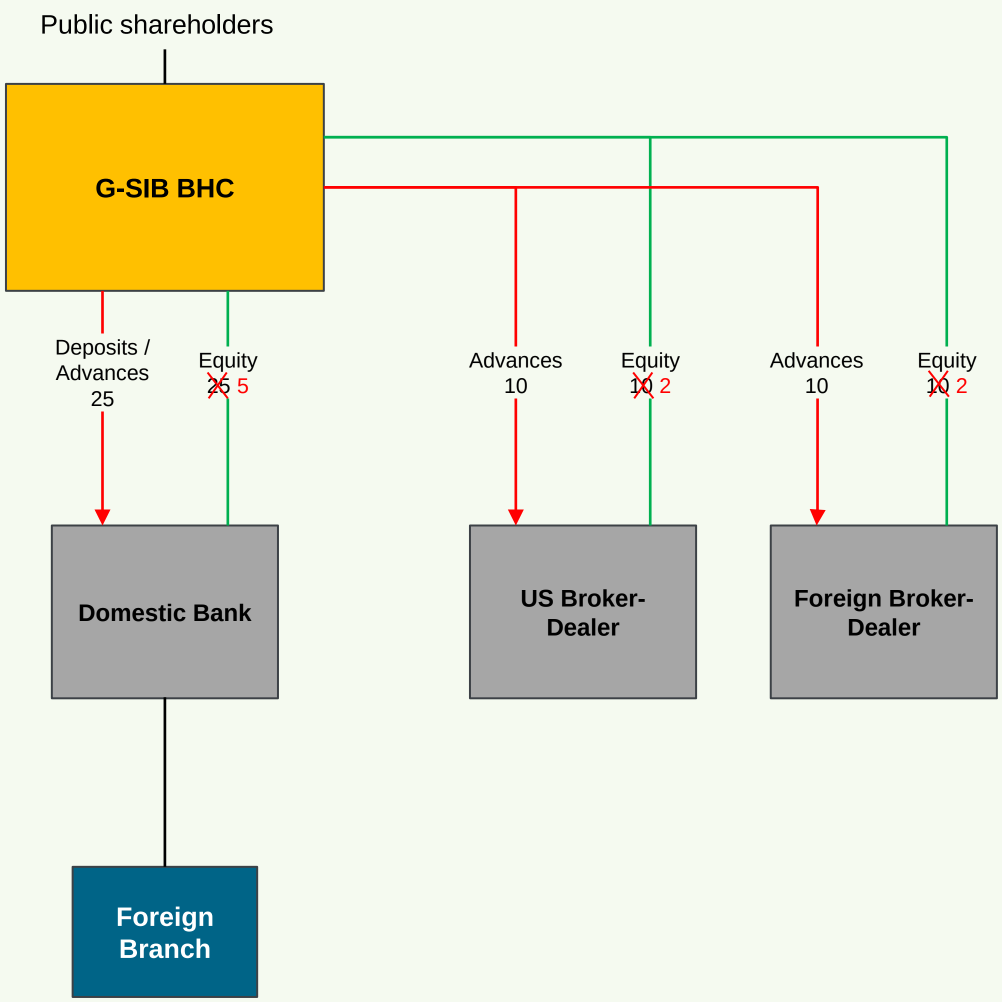
Appendix A: Step-by-Step Illustration of SPOE Resolution

Hypothetical Losses Resulting in Failure

- Total hypothetical losses: 41
- Model assumes losses are spread evenly among operating subsidiaries
- Model assumes that failure is based on the likely inability of the G-SIB BHC to pay its obligations as they come due in the ordinary course of business because of insufficient liquidity or access to liquidity as a result of the losses
- Red font indicates figures that changed as a result of losses

Parent Only Balance Sheet

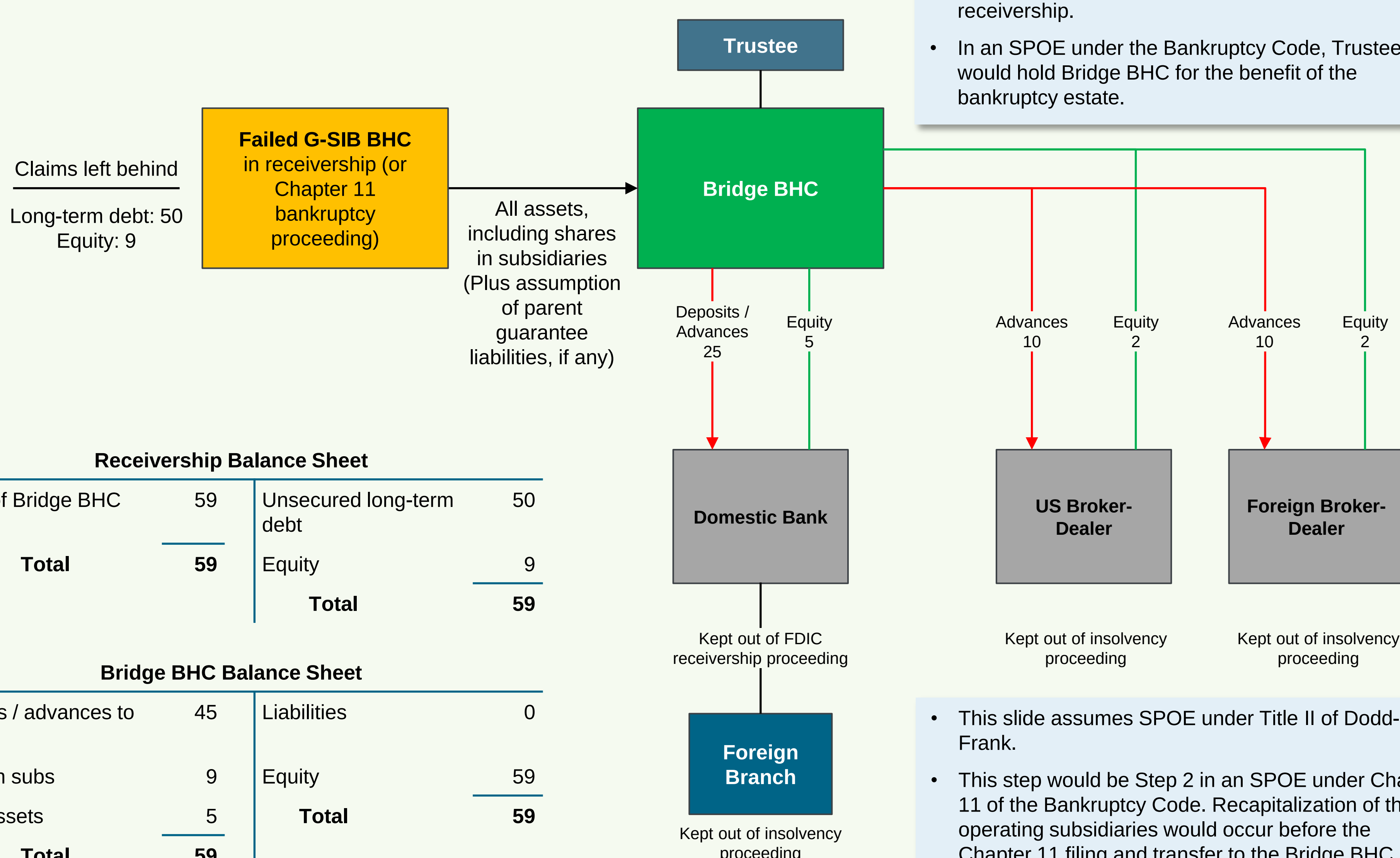
Deposits / advances to subs	45	Unsecured long-term debt	50
Equity in subs	**9**	Unsecured short-term debt	0
Other assets	**5**	Secured liabilities	0
Total	**59**	Other liabilities	**0**
		Equity	**9**
		Total	**59**



Appendix A: Step-by-Step Illustration of SPOE Resolution

Step 1: Recapitalizing Business Transferred to Bridge BHC

- Trustee holds Bridge BHC for the benefit of the receivership.
- In an SPOE under the Bankruptcy Code, Trustee would hold Bridge BHC for the benefit of the bankruptcy estate.



Receivership Balance Sheet

Equity of Bridge BHC	59	Unsecured long-term debt	50
Total	**59**	Equity	9
		Total	**59**

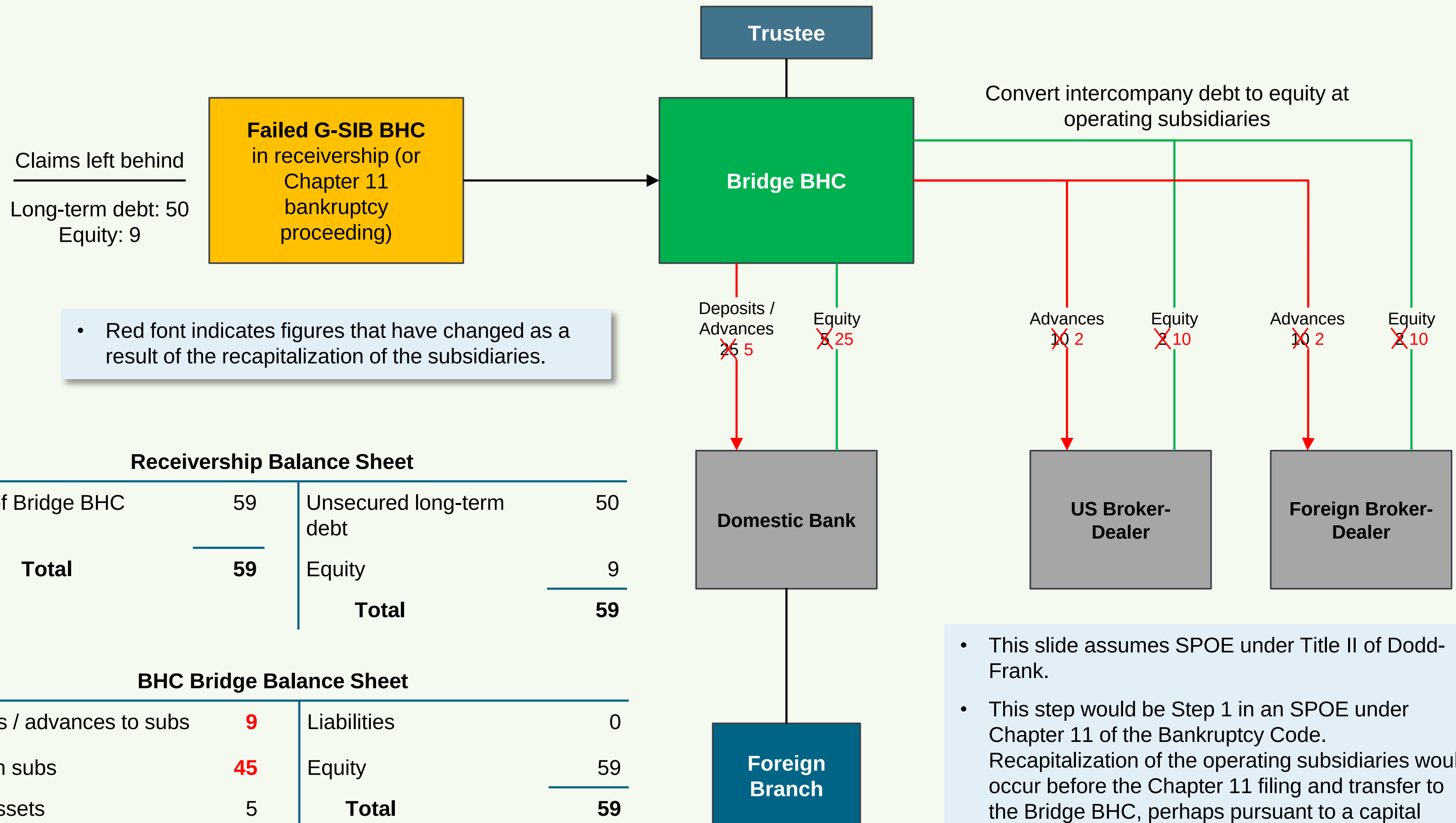
Bridge BHC Balance Sheet

Deposits / advances to subs	45	Liabilities	0
Equity in subs	9	Equity	59
Other assets	5	**Total**	**59**
Total	**59**		

- This slide assumes SPOE under Title II of Dodd-Frank.
- This step would be Step 2 in an SPOE under Chapter 11 of the Bankruptcy Code. Recapitalization of the operating subsidiaries would occur before the Chapter 11 filing and transfer to the Bridge BHC, perhaps pursuant to a capital contribution agreement.

Appendix A: Step-by-Step Illustration of SPOE Resolution

Step 2: Recapitalizing Operating Subsidiaries



- Red font indicates figures that have changed as a result of the recapitalization of the subsidiaries.

Receivership Balance Sheet

Equity of Bridge BHC	59	Unsecured long-term debt	50
Total	**59**	Equity	9
		Total	**59**

BHC Bridge Balance Sheet

Deposits / advances to subs	**9**	Liabilities	0
Equity in subs	**45**	Equity	59
Other assets	5	**Total**	**59**
Total	**59**		

- This slide assumes SPOE under Title II of Dodd-Frank.
- This step would be Step 1 in an SPOE under Chapter 11 of the Bankruptcy Code. Recapitalization of the operating subsidiaries would occur before the Chapter 11 filing and transfer to the Bridge BHC, perhaps pursuant to a capital contribution agreement.

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Appendix A: Step-by-Step Illustration of SPOE Resolution

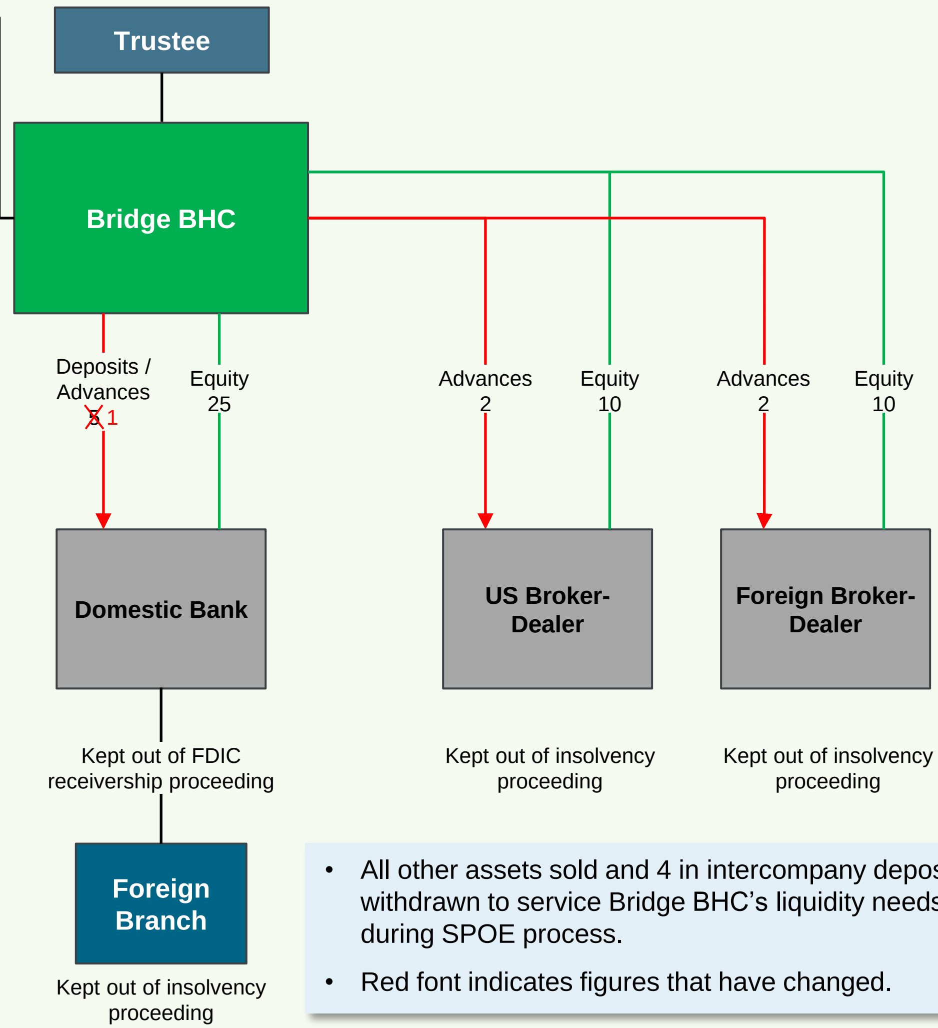
Step 3: Distribution of Equity (or Net Proceeds from Sale) in Satisfaction of Claims

- Unsecured long-term debt claimants receive Bridge BHC shares worth 50 (or the net proceeds from a public or private sale) in satisfaction of their claim for 50
- Equity: 0

Claimants

Failed G-SIB BHC in receivership (or Chapter 11 bankruptcy proceeding)

Shares in Bridge BHC (or net proceeds from sale) distributed to left-behind claimants in satisfaction of claims in accordance with the priority of their claims



Receivership Balance Sheet (Revalued)

Equity of BHC Bridge	50	Unsecured long-term debt	50
Total	50	Equity	0
		Total	50

BHC Bridge Balance Sheet (Revalued)

Deposits / advances to subs	5	Liabilities	0
Equity in subs	45	Equity	50
Other assets	0	**Total**	50
Total	50		

- All other assets sold and 4 in intercompany deposits withdrawn to service Bridge BHC's liquidity needs during SPOE process.
- Red font indicates figures that have changed.

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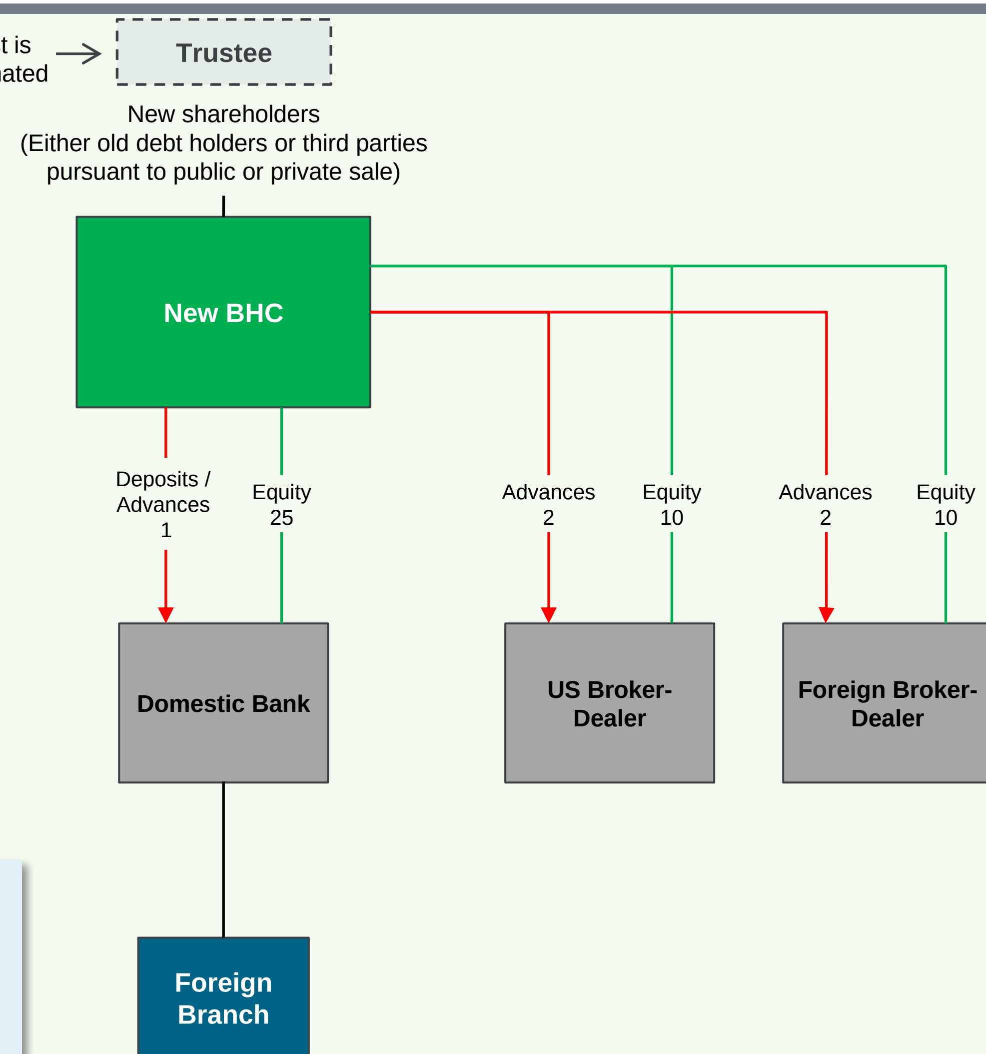
Appendix A: Step-by-Step Illustration of SPOE Resolution

Step 4: Termination of Bridge Status

Trust is terminated



Failed G-SIB BHC in receivership (or Chapter 11 bankruptcy proceeding)

Bridge BHC converts into New BHC (loses status as a bridge institution)

New BHC Balance Sheet

Deposits / advances to subs	5	Liabilities	0
Equity in subs	45	Equity	50
Other assets	0	**Total**	**50**
Total	**50**		

- In this example, the new BHC that exits SPOE has half the balance sheet of the failed G-SIB BHC that entered SPOE. Indeed, the BHC that exits SPOE is virtually always substantially smaller than the BHC that entered SPOE because of losses and the sale of assets to provide liquidity during the SPOE process. See public summaries of 2015 Title I Resolution Plans of the G-SIB BHCs, which you can access here.

Appendix B: Calculation of External TLAC Buffer Level

Appendix B: Calculation of External TLAC Buffer Level
(Hypothetical Examples)

Redundancy with Existing Capital Requirements: Although the external TLAC buffer must be composed entirely of CET1, the proposal would not require G-SIB BHCs that already satisfy their capital buffer requirement applicable under existing capital rules to issue any additional CET1.

- The same CET1 used to satisfy the capital conservation buffer may be used to satisfy external TLAC and external TLAC buffer requirements.
- The firm's capital buffer requirement will always be greater than or equal to its external TLAC buffer requirement:

Capital Buffer Requirement:
2.5% +
max {Method 1 G-SIB Surcharge, Method 2 G-SIB Surcharge}

≥

External TLAC Buffer Requirement:
2.5% +
Method 1 G-SIB Surcharge

- As illustrated by Scenarios A and B to the right, any shortfalls from TLAC may be met with instruments other than CET1 if the capital conservation buffer is already satisfied. In Scenario B, the firm's actual external TLAC risk-based ratio is increased through the issuance of additional external LTD rather than CET1.

For analytical simplicity, a 2.5% G-SIB surcharge is assumed under both method 1 and 2, creating a total applicable firm-specific buffer of 5% under both capital and TLAC rules:

Level of Firm's Actual Capital, External TLAC and External LTD, each as Percentage of RWAs (assumed)

Capital / LTD Category	Scenario A	Scenario B
CET1*	10.5%	10.5%
AT1*	1.0%	1.0%
T2**	2.0%	2.0%
Other eligible LTD	9.0%	10.0%

Scenario A: Shortfall to Required Buffer

Ratio	Required Minimum Ratio	Firm's Actual Ratio	Firm's Actual Buffer (CET1)	Excess / (Shortfall) over Required Buffer
CET1 Risk-based Ratio	4.50%	10.50%	6.00%	1.00%
Tier 1 Risk-based Ratio	6.00%	11.50%	5.50%	0.50%
Total Capital Risk-based Ratio	8.00%	13.50%	5.50%	0.50%
External TLAC Risk-based Ratio	18.00%	22.50%	4.50%	(0.50)%
External LTD Risk-based Ratio	11.00%	11.00%	N/A	

Scenario B: Required Buffer Satisfied

Ratio	Required Minimum Ratio	Firm's Actual Ratio	Firm's Actual Buffer (CET1)	Excess / (Shortfall) to Required Buffer
CET1 Risk-based Ratio	4.50%	10.50%	6.00%	1.00%
Tier 1 Risk-based Ratio	6.00%	11.50%	5.50%	0.50%
Total Capital Risk-based Ratio	8.00%	13.50%	5.50%	0.50%
External TLAC Risk-based Ratio	18.00%	23.50%	5.50%	0.50%
External LTD Risk-based Ratio	11.00%	12.00%	N/A	

* We have assumed that all CET1 and AT1 would be recognizable as eligible TLAC.

** We have assumed that all T2 would be recognizable as LTD.