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Cabinet News and Views

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Long-Term Debate

August 31, 2023

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In This Issue ...

This week, we're shining a spotlight on a significant move by the Federal Deposit Insurance Corporation, Federal Reserve Board, and the Office of the Comptroller of the Currency. Federal banking agencies have jointly proposed a long-term debt requirement that could reshape the landscape for large banks – those with assets of $100 billion or more, but not a GSIB. I also dive into the rest of the agenda of the FDIC Board meeting from Tuesday.

My colleague Alix Prentice discusses the recent shifts in trading rules and regulatory changes under the new Financial Services and Markets Act 2023.

Any comments or questions? Just drop me a note here.

Daniel Meade
Editor, *Cabinet News and Views*

The Three Federal Banking Agencies Propose Long-Term Debt Requirement for All Large Banking Organizations

By **Daniel Meade**
Partner | Financial Regulation

The Federal Deposit Insurance Corporation ("FDIC"), Federal Reserve Board ("FRB") and Office of the Comptroller of the Currency ("OCC") (together, the "Agencies") issued a proposed rule (the "LTD NPR") to require large banks (generally defined as those with $100 billion or more in assets) to issue and maintain minimum amounts of long-term debt ("LTD").

The issuance of the LTD NPR had been at least mentioned as a policy possibility since at least last April with Acting Comptroller of the Currency Michael Hsu's remarks at the Wharton Conference on Financial Regulation in April (which we discussed at the time). The FRB and FDIC then issued an Advanced Notice of Proposed Rulemaking ("ANPR") titled "Resolution-Related Resource Requirements for Large Banking Organizations" in October of last year (which we discussed at the time as well). FDIC Vice Chair Travis Hill mentioned the idea in the wake of the three regional bank failures in March and April of this year. FRB Vice Chair of Supervision Michael Barr included an LTD requirement for large banking organizations in his report following his holistic capital review last month, and most recently, FDIC Chair Martin Gruenberg discussed the LTD requirement two weeks ago.

The LTD NPR, if finalized, would require large banking organizations that are not already subject to the total loss-absorbing capacity ("TLAC") requirements for U.S. global systemically important banks ("GSIBs") to maintain a minimum amount of LTD to serve as an additional layer of protection to absorb losses. The Agencies assert that had this LTD requirement been in place this spring, it likely would have given the FDIC more options in resolving the three large regional banks, and reduced costs to the Deposit Insurance Fund.

Under the LTD NPR, the LTD requirement is calibrated as requiring a minimum amount of eligible long-term debt equal to the greater of 6% of risk-weighted assets, 3.5% of average total consolidated assets, and for banks subject to the supplementary leverage ratio, 2.5% of total leverage exposure under the supplementary leverage ratio. Much like the TLAC requirements, the LTD NPR would require that the LTD be "plain vanilla" so that, among other things, it is subordinated to depositors and other unsecured credits, has a maturity of more than a year (with a 50% haircut for instruments with a maturity between one and two years), has minimal acceleration or credit-sensitive features.

Comments on the proposal are due by November 30. That is the same day that comment are due on the Basel III Endgame rules the Agencies proposed a month ago (as well as a number of other proposals the FDIC Board considered Tuesday). FRB Governor Michelle Bowman noted the multiple outstanding proposals as one of her concerns with the proposal she mentioned in her statement. Trade groups such as the Bank Policy Institute and the American Bankers Association aren't

waiting until November 30 to air some of their criticism of the proposal. They criticize the proposal as being too costly without providing worthwhile benefits, and for not following the tailoring regimes that have been established.

With so many proposals with a November 30 comment deadline, it's looking like many of the proponents of a friendly neighborhood bank regulatory policy might be working through Thanksgiving this year.

FDIC Board Meeting Tackles a Meaty Agenda

By **Daniel Meade**
Partner | Financial Regulation

In addition to approving the long-term debt proposal ("LTD NPR") we discuss in another article this week, the Federal Deposit Insurance Corporation ("FDIC") Board had a busy day on Tuesday. As we noted last week, when the FDIC provided notice for the board meeting, Tuesday's meeting was a busy one.

In addition to the LTD NPR, the FDIC (together with the Federal Reserve Board ("FRB")) issued proposed guidance on the filing of resolution plans (AKA living wills) required under section 165(d) of the Dodd-Frank Act. The guidance would apply to bank holding companies and foreign banking organizations with more than $250 billion in assets that aren't already subject to the Global Systemically Important Bank ("GSIB") Guidance issued in 2019 (basically Category II and III institutions as defined in the 2019 tailoring rule). The proposed guidance for Category II and III is largely consistent with the GSIB Guidance. Thus much of the proposed guidance does seem to presume a single point of entry ("SPOE") approach to the resolution plans. Nevertheless, the proposed guidance does note that institutions are free to choose their approach and the proposed guidance does give some nods to institutions that have multiple point of entry ("MPOE") plans. Notwithstanding the statement in the proposed guidance that large banking organizations are free to choose between MPOE and SPOE, there does seem to be an unstated preference for SPOE. Comments are due November 30.

The FDIC Board also issued a proposed rule for plans for large insured depository institutions with at least $100 billion in assets ("the IDI Plan Proposal"). As part of the proposal, IDIs between $50 billion and $100 billion in assets would need to file "more limited" informational filings. The IDI plans have some similarities to the 165(d) plans, but often are focused on actions to prevent the failure of the banks rather than to wind it up. Having said that, the proposal would require more information to be reported with the FDIC as the FDIC realized with this spring's failures that more information may have given the FDIC more optionality in resolving those three large banking organizations.

All of the proposals regarding resolvability of large banking organizations would seem to have the effect of weakening the tailor that had occurred in the last few years. Citing such lack of tailoring, Vice Chair Hill and Director McKernan voted against the proposed IDI rule.

The FDIC Board also approved updating its internal governance with regard to sales of failed IDIs with $50 billion or more in assets. This topic was the most interesting issue of the meeting for fans of parliamentary procedure. The issue, as a whole, seems to have come up at Director McKernan's impetus, as he noted that the sale of substantially all of First Republic Bank was an action that did not need FDIC Board approval. To address Director McKernan's question about more Board involvement in sales of assets out of receivership, the procedures that did pass do require more information to be shared by staff with the Board, and gives the Board

a mechanism to require a vote of the Board if a majority of the Board asks for it, but do not mandate a Board vote. Director McKernan offered his preferred approach as an amendment in the nature of a substitute to the proposal by staff. Director McKernan's amendment failed in a 3-2 vote. The change to FDIC procedures passed on a 4-1 vote with Director McKernan voting against. Wherever one might land on the competing policy positions, the debate did at least show a well-functioning Board.

Changes to Trading Rules Now Effective Under New Financial Services and Markets Act 2023

By **Alix Prentice**
Partner | Financial Regulation

The Financial Services and Markets Act 2023 ("FSMA 2023") became law on 29 June 2023, with its principal objective stated in Section 1 being the revocation and replacement of EU laws that were retained and on-shored into the UK after its departure. Understandably, this process is subject to a phased approach with much being revoked by 1 January 2024.

However, some 100 transitional provisions have now become effective in order to give effect to specific transitional provisions in FSMA 2023 pending, in most cases, the eventual replacement by regulator-made rules. These include the following changes to the UK version of the Markets in Financial Instruments Directive.

1. Removing the share-trading obligation: Effective from 29 August 2023, UK firms will no longer be bound by the provisions of Article 23 of the UK version of the Markets in Financial Instruments Regulation ("UK MiFIR") requiring them to trade certain shares on a UK venue.
2. Amendments to the derivatives trading obligation: Effective from 29 August 2023, UK MiFIR will be amended to align the universe of in-scope counterparties with that of the UK version of the European Markets Infrastructure Regulation ("UK EMIR") as it applies to the clearing obligation.
3. Removing the double volume cap mechanism ("DVC"): Effective from 29 August 2023, the limitation on the use of equity waivers under the existing reference price waivers or the DVC will be removed.

Note that as of 29 August 2023, the FCA has varied or removed relevant transitional directions and policy statements that apply to these items.