Regulatory brief

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Resolution planning: A public peek into the plans

Overview

Last week, the Federal Reserve and the FDIC released the public sections of the second annual resolution plans filed by 11 Category 1 firms (i.e., financial institutions with $250 billion or more in US nonbank assets). The regulators had extended the deadline from July 1st to October 1st, in recognition of the firms' need for additional time to incorporate guidance published in April (the "April Guidance").[1]

The plans have evolved since the first versions were submitted in July 2012. First, and most notably, all but two of the 11 plans identified more Material Entities than they included in 2012. Second, many of the public sections indicated that the firms considered additional resolution strategies, including a "single point of entry" approach. Although resolution strategies are not fully explored within the public sections, many firms have availed themselves of the options provided by the April Guidance to present feasible resolution strategies that assume the idiosyncratic failure of the parent firm without the requirement that all Material Entities also fail.

What has not evolved is that the plans' public sections continue to be very short (i.e., under 50 pages) as compared to the actual plans themselves which run thousands of pages. Relative to the plans themselves, the public sections reveal limited information, and what is revealed makes the plans seem more alike than they actually are. This generic nature is in part due to the public sections' brevity, but the driving reasons are firms' competitive concerns and the reality that resolution plans can be politicized (with press headlines and congressional scrutiny of "too big to fail" frequently re-emerging).

This **Financial Services Regulatory Brief** (a) analyzes the public sections of the Category 1 firms' plans, particularly with respect to added material entities and new strategies, and (b) provides our view of what firms should be preparing for next.

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[1] See PwC's *Financial Services Regulatory Brief, Resolution Planning – new guidance, more time, no specificity* (April 2013).

Expanded coverage through new material entities

Compared to the 2012 public sections, nine of the 11 Category 1 firms added Material Entities while two decreased their number of Material Entities, as depicted in the below table.

Comparison of resolution plan public sections for Category 1 filers – by Material Entities

	Material Entities				Material Entities		
US Institutions	2012	2013	+/-	**Foreign Institutions**	2012	2013	+/-
Bank of America	7	21	14	Barclays	6	9	3
Citigroup	17	27	10	Credit Suisse	16	23	7
JPMorgan Chase	25	35	10	Deutsche Bank	7	8	1
Goldman Sachs	22	25	3	UBS	11	10	(1)
Morgan Stanley	18	17	(1)				
Bank of New York Mellon	14	15	1				
State Street	11	16	5				

Specifically, nine firms added an average of six Material Entities, with three firms adding 10 or more. This addition of Material Entities by nine of the 11 institutions is significant because the full, confidential portion of the plans must include detailed information and bespoke resolution plans for each entity deemed material. These detailed data requirements and bespoke resolution strategies should significantly expand the size of the 2013 resolution plans (versus the 2012 plans).

Across the 11 Category 1 firms, the new Material Entities generally fall into one of two categories: (a) foreign bank branches, or (b) service companies providing technology, staff, or real estate. These additions result from the April Guidance's clarification of factors to be considered in determining materiality which focused on the importance of identifying each entity necessary for maintaining day-to-day operations of a core business line or critical operation, including those subsidiaries or foreign offices that (a) support global treasury operations funding or liquidity activities, (b) provide material operational support in resolution, or (c) are engaged in derivatives booking activity either internally or client-facing.

With respect to the two firms that reduced their number of Material Entities, the reduction in one case was due to an internal legal entity merger, and the other was due to a change in business focus within a core business line. In the future, we anticipate that the 11 firms could modestly reduce the number of their Material Entities as a result of additional internal mergers.

For their upcoming annual filings[2], Category 2 and 3 firms[3] should give careful consideration to the April Guidance with regards to the identification of Material Entities, if they have not already. Any significant expansion of Material Entities, if necessary, will likely require additional resources to ensure that all resolution plan requirements for each Material Entity are fulfilled. Just as the Category 1 firms appear to have broadened the scope of entities deemed material in their second annual plans, some Category 2 and 3 institutions are likely to also discover the need to add Material Entities, albeit to a lesser degree, as they analyze the operational and financial interconnections of their core business lines and critical operations.

New strategies

Resolution plans created under section 165(d) of Dodd-Frank must assume the failure of the parent firm. For the first Category 1 annual plans submitted in 2012, the regulators also required the firms to include a resolution strategy that assumed the failure of all Material Entities. For their 2013 filings, the April Guidance offered additional permissible resolution strategies, including several that still require the bankruptcy (or other applicable resolution mechanism) of the parent firm but not all Material Entities.

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[2] Category 2 firms' second annual filings and Category 3 firms' first annual filings are due by July 1, 2014 and December 31, 2013, respectively.

[3] Category 2 firms are generally those with total US nonbank assets between $100 billion and $250 billion; Category 3 firms are generally those with total US nonbank assets of less than $100 billion.

One type of resolution strategy that falls within the April Guidance is the single point-of-entry ("SPE") approach, which is the subject of considerable attention as global regulators explore the feasibility of resolving major financial institutions through the "bail-in" of equity and debt holders to facilitate the continued going concern of operating subsidiaries.[4] While most of the firms indicated in their second filing that their plan considered a combination of different resolution strategies including the sale of operating entities or businesses, several firms specifically indicated consideration of the SPE approach.

However, in the words of one institution, the SPE approach may require "certain changes to the [US] bankruptcy code and other laws and regulations." Nevertheless, it is clear that the US and international regulators are giving increased attention to the SPE approach, or possibly a hybrid multiple point-of-entry approach (i.e., where some entities are recapitalized and continued, while others enter resolution proceedings and are liquidated or wound down). A key requirement to the success of any SPE approach is the existence of sufficient resources that may be "bailed-in" (i.e., converted to equity). US regulators are expected to propose requirements for bail-in capital later this year.[5]

[4] See PwC's *Financial Services Regulatory Brief, Proposed US/UK resolution strategy – more questions than answers* (December 2012).

Other observations

The required content for the public section is prescribed by section 165(d), and most of the Category 1 filers drafted the public elements of their plan in the order discussed within 165(d). As was true in 2012, some institutions added a discussion of their improved financial strength since 2008 (although this section was generally much shorter than was the case in 2012).

The table below summarizes a few other notable trends with respect to these public elements. For example, most institutions indicated that their full resolution plans include more than one strategy. A number of institutions also made mention of their recovery plans, suggesting a trend toward better convergence of recovery and resolution planning in the US.

[5] See PwC's *Financial Services Regulatory Brief, Basel & prudential standards: US moving faster than world* (August 2013).

Comparison of resolution plan public sections for Category 1 filers – by elements of public section

	Bank of America	Citigroup	JPMorgan Chase	Goldman Sachs	Morgan Stanley	BNY Mellon	State Street	Barclays	Credit Suisse	Deutsche Bank	UBS
Number of Material Entities (2013)	21	27	35	25	17	15	16	9	23	8	10
Number of Material Entities (2012)	7[6]	17	25	22	18	14	11	6	16	7	11
Core Business Lines (2013)	5	15	26	4	3	4	2	5	12	10	5
Core Business Lines (2012)	5	15	30	2	3	4	2	4	11	10	7
Pages (2013)	34	31	31	31	23	24	23	27	15	29	31
Pages (2012)	42	31	31	32	20	24	22	14	15	29	25
Strategies discussed (2013)	3	2	2	3	1	2	3	2	2	2	1
Discusses financial strengthening since 2008 (2013)	Y	Y	N	N	Y	N	N	Y	N	N	N
Mentions SPE (2013)	Y	Y	Y	N	N	Y	Y	Y	Y	N	N
Mentions use of bridge bank or recapitalizations of certain MEs (2013)	Y	Y	Y	Y	N	Y	Y	Y	N	Y	N
Mentions Recovery Plan (2013)	N	N	Y	Y	Y	N	Y	Y	Y	N	N

[6] The firm's public section stated that their plan "included but was not limited to seven Material Entities."

Moving forward

The next annual resolution filing deadline for the 11 Category 1 firms is July 1, 2014, which leaves them with less than nine months to prepare. In the 2014 plans, the US regulators undoubtedly want to see filers identify additional opportunities to make resolution faster and easier. Because some factors to improve resolvability are outside the firms' control (e.g., changes in bankruptcy code, laws, or regulations), firms should focus on showing progress on those that support the feasibility of their resolution strategies which are within their control.

These factors might involve (a) improving the accuracy and completeness of information on operational and financial interconnections, (b) enhancing the level of detail in service agreements and service level agreements, (c) accelerating the speed for assembling required information, and (d) further clarifying system ownership and licensing, especially for applications developed in-house.

Regulators seem intent on providing firms with feedback on their second annual filings; however, any meaningful feedback will very likely remain oral. Regulators continue to evaluate what they want (and must agree among themselves), and – like the banks – face the reality of a politically charged environment.

Additional information

For additional information about PwC's Financial Services Regulatory Practice and how we can help you, please contact:

Dan Ryan
Financial Services Regulatory Practice Chairman
646 471 8488
daniel.ryan@us.pwc.com

Alison Gilmore
646 471 0588
alison.gilmore@us.pwc.com

Contributors: Sally Neal and Sharon Haas.

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