Remarks as Delivered by Michael Helfer, Vice Chairman, Citigroup,
July 26, 2012
***Navigating Transformational Change of the Global Financial Landscape* Opening Dinner**
Bretton Woods Committee, Deloitte, University of Maryland Smith School

Thank you very much.

I have learned one important lesson already from this conference: if Nancy Jacklin calls you up and invites you to participate in a conference, make sure you ask her what role she has in mind. I did not think I was signing up to be the keynote speaker! It is quite an honor be to asked to address this distinguished group.

We all share the goal, as stated by the organizer of this conference, of "preventing future financial disasters, ensuring long-term stability of global financial markets, and promoting a resilient, innovative and profitable financial industry."

The question we all face is: How do we achieve those goals? While these goals are not mutually exclusive, there are some tensions among them, and achieving all of them will require rigorous analysis and bold thinking about what will work and what won't work – something that is not always readily available in this town in a year evenly divisible by four.

We at Citi have been thinking about these issue a great deal over the past few years. We faced our own challenges during the financial crisis, more than some institutions, less than others, and that experience gives us a perspective, I believe, on solutions that will work.

We have been strong proponents of legislative and regulatory financial reform. We believe that financial reform needs to the centered on three core principles: risk-based capital requirements, liquidity standards, and resolution mechanisms. Getting these three right is critical – I do not say easy – but if we get them right then the safety and soundness of the financial system as a whole can be protected while at the same time "Too Big To Fail" will be eliminated once and for all.

I will concentrate today on resolution issues. These issues are very much on my mind because, as you know, the country's largest banking institutions submitted their first "resolution plans" under Dodd-Frank earlier this month. Ours ran 2300 pages or so, and I am told it was not the longest one submitted. So the regulators will have plenty of information to review as they consider their responses and requests for additional.

For statutory and regulatory reasons, the resolution plans just submitted had to assume that all material legal entities within the bank holding company fail simultaneously and that the holding company files a petition in bankruptcy. Put another way, the plans have to assume a so-called "Title I" failure, involving the holding company filing a petition in bankruptcy in a bankruptcy court. The plans also have to assume an idiosyncratic failure rather than a systemic crisis. That is, each bank was required to assume that something unique but unidentified has caused it, and only it among its competitors, to fail.

Some have asked whether these assumptions are realistic and if they are not, what is the value of these resolution plans – plans that took hundreds of thousands of hours and cost millions of dollars to prepare.

Remarks as Delivered by Michael Helfer, Vice Chairman, Citigroup,
July 26, 2012
***Navigating Transformational Change of the Global Financial Landscape* Opening Dinner**
Bretton Woods Committee, Deloitte, University of Maryland Smith School

Dwight Eisenhower famously said that while plans are nothing, planning is everything. I am told that the plan for the D-Day invasion ran into the thousands of pages, and that if you compare what was written to what actually happened at Normandy on June 6th, 1944, you'd find a great deal that did not look anything like the plan. Yet because of that plan, everyone had information and a clear mission. Everyone knew what was expected of him and his unit. Everyone knew the lay of the land and the disposition of nearby allied forces. Thus, when things did not go according to plan—which was often—they had a basis for action.

Financial institution policy and banking supervision are not anything like a real war, despite the metaphors about "incoming shells" and "foxholes" we all used during the financial crisis. But I would suggest that, at a minimum, the resolution planning that has just been done has the same kind of value for institutions and their supervisors that General Eisenhower said his invasion planning had for him.

The resolution plans provide the regulators and the institutions themselves with information about the legal structure, business operations, technology resources, foreign operations, and much more, including reams of financial information broken down by core business line. This information, updated and in a consistent form, is the information the regulators will need readily at hand in the event a resolution is ultimately necessary. In the event of an actual resolution scenario, it is unlikely that the institution and all its material subsidiaries will be wound down exactly as its resolution plan sets out. But the plan itself, particularly as it evolves over time based on interaction between the regulators and the institutions, will be an invaluable and immediate source of vital information to be used in the event of a failure.

Let me give you just one small example of something that the resolution plans brought into sharp focus for institutions and regulators alike: legal entity structure at large holding companies. The process of preparing the resolution plans made very clear to all of us that reducing the number of legal entities, simplifying the legal entity structure, centralizing the provision of information security and technology services in the right legal entity, assuring that inter-company service level agreements are complete, current and immediately available – all these and more legal entity housekeeping tasks are critical for the prompt and effective resolution of any large institution with multiple legal entities – which is to say, any large bank holding company. It isn't sexy, and take it from me, doing this right is isn't the single most fun way to spend your time, but it is essential.

The resolution plans also bring into focus, once again, questions about market structure. In particular, planning for resolution has reinforced our long-held position in favor of central clearing of third-party derivatives and moving as many derivative transactions to exchanges as feasible. These are good things to do, in our view, to increase systemic stability and market efficiency. When you add on top of that the benefits of central clearing and exchanges from the perspective of limiting the disruptive effect of the failure of a large banking institution, the argument becomes even more persuasive.

Remarks as Delivered by Michael Helfer, Vice Chairman, Citigroup,
July 26, 2012
***Navigating Transformational Change of the Global Financial Landscape* Opening Dinner**
Bretton Woods Committee, Deloitte, University of Maryland Smith School

There is another aspect of resolution planning that is, perhaps, even more important in the long run than the resolution plans just submitted under Title I of Dodd-Frank – but which will build on the information in those plans. That is Title II of Dodd-Frank – the Orderly Liquidation Authority chapter. Title II grants the FDIC for the first time the power to take over the failing holding company of a bank as swiftly as the FDIC has, for many years, been able to take over the failing bank itself. If the FDIC uses its Title II authority to take over a holding company, the holding company will not have to enter bankruptcy proceedings, with all of the delay, uncertainty – and lawyers -- associated with the bankruptcy of a major financial institution. We tried the judicial bankruptcy process when Lehman Brothers failed, and I do not think anyone would describe the process or consequences as satisfactory – except perhaps the bankruptcy lawyers involved.

The FDIC has described generally the way a Title II resolution could work, and its outline is, in my view, very sensible. In short, when the bank subsidiary of a large bank holding company sustains losses that threaten organization's viability, the bank holding company would provide additional capital to the bank to offset these losses. As a result, the bank would be recapitalized and therefore viable; in other words, the bank would not fail. The holding company would fail and under its new authority the FDIC would create a bridge holding company, much like it does when a bank fails and the FDIC creates a bridge bank. The effect of this plan is to impose the cost of the failure on the holding company's shareholders and creditors, rather than on the deposit insurance fund, the government or the taxpayers. More specifically, holding company shareholders would bear the losses first and one would expect that they will be wiped out; holding company creditors will likely bear losses as well, and would receive equity in the newly reorganized holding company in place of the debt, reflecting the value of what remains in the holding company. A new board and management would be put in place.

This approach, sometimes called the "single point of entry" holding company approach, is very sensible, principally because it provides a way for the subsidiary bank to stay solvent and operating, while only the holding company fails. This approach is systemically protective because the holding company itself, by definition, does not have any deposits. In addition, holding companies typically do not themselves issue swaps and other sorts of derivatives; and they typically don't operate themselves directly – as opposed to owning subsidiaries -- in foreign countries. As long as the subsidiary bank stays solvent and operating, even if the holding company fails, there is no reason for disruptive bank runs, no messy defaults on derivatives, and no issues about depositor preference. The bank's customers and clients continue to be served as they were before the holding company failed. And in a Title II resolution as envisioned by the FDIC, international cooperation relating to foreign branches of the US bank should be significantly easier for all regulators concerned.

I want to stress this last point. The use by the FDIC of its Title II authority will, I believe, substantially mitigate the obstacles that could otherwise exist to international cooperation, because the subsidiary bank will remain solvent and operating. I believe that the further development on the part of regulators of details about how a Title II resolution would work will lead to increased understanding and recognition of the value of the FDIC's Title II approach in

the US and in foreign countries. Over time, I am optimistic that Title II can alleviate many if not all of the very legitimate concerns that non-US regulators understandably have about the impact of US resolution mechanisms on depositors and creditors of branches of US banks in the host country and on the host country economy in general.

Title II has been criticized recently as being itself a "bail out" and a perpetuation of "too big to fail." I believe that criticism is unwarranted.

The "bail-out" charge arises from the fact that Title II authorizes temporary government funding for the new bridge holding company if it is needed and otherwise not available. But Title II flatly prohibits taxpayer funds from being used to pay for losses in failed banking institutions. Orderly liquidation funding can be provided only if the government is fully protected by the unencumbered assets of the institution. If that turns out not to be the case, there will be claw-backs against creditors who were overpaid, and ultimately a levy on the largest financial institutions to reimburse the government. As a result, there can be no "taxpayer bailout" under Title II – precisely because care was taken by Congress to assure there would no cost to the taxpayers.

And a Title II resolution most definitely is a "failure" in which the consequences of failure would be, as they should be, visited on the stockholders, unsecured debt holders and management of the failed institution. It is, at the holding company level, the same kind of "bridge" structure that the FDIC has had authority to use – and has used – at the subsidiary bank level for many years. And the fact that it does not involve lengthy and complex bankruptcy court proceedings is, I submit, an advantage, not a flaw.

A related issue under Title II is of course the capital structure of bank holding companies. Orderly Liquidation Authority, as envisoned by the FDIC, works because there is unsecured debt at the holding company that can be converted into equity as a key step in the resolution process. Large US bank holding companies generally have sufficient unsecured debt on their balance sheets to handle losses well in excess of those actually incurred in the financial crisis or hypothesized in regulatory stress tests. But if Title II is to be effective, the management and Board's of banking institutions – and their regulators – will have to keep a close eye on the unsecured debt levels at the holding company level. In other words, management and Boards will have to take into account when making decisions about levels of unsecured debt not just all the factors that have traditionally informed these decisions, but also now the additional factor of the impact of debt levels on resolvability under Title II. And any institutions that do not have enough such debt, and their regulators, will have to formulate resolution or other strategies to deal with this issue.

This and other issues relating to Title II will benefit from the further work the FDIC is doing and from further consultations with non-US regulators and input from the industry. I believe it would be very useful for all concerned, including the industry, policy-makers, and foreign regulators, if, when it is ready to do so, the FDIC proposes and, after notice and public comment, adopts a regulation or policy statement describing more precisely the circumstances in which it would

Remarks as Delivered by Michael Helfer, Vice Chairman, Citigroup,
July 26, 2012
***Navigating Transformational Change of the Global Financial Landscape* Opening Dinner**
Bretton Woods Committee, Deloitte, University of Maryland Smith School

invoke Title II and how a Title II resolution would work. The result would be a more formal set of rules or regulatory policies than we now have. This would provide additional clarity and certainty about Title II to investors, other regulators and the public, as well as the industry.

Finally, let me say a few more words about transparency. You will not be surprised to hear me endorse Vikram's proposal, presented to you last fall, to establish a benchmark portfolio. Since you've heard it, I won't belabor it.

But in brief, investors need a way to price risk that looks beyond disclosed capital ratios, which do not reveal enough information about how particular classes of assets were risk-weighted. Vikram suggested that the way to create more transparency would be to require all financial institutions—not just banks—to run their risk measurements against a standardized and fully public benchmark portfolio of assets representative of the classes of assets that banking institutions actually have on their balance sheets. This would give investors a basis for "apples to apples" comparisons between financial institutions.

Our organizers said they want to "identify actions" that would increase the prospects of achieving the goals I quoted at the beginning of my talk. So let me give you three specific things we all can do:

- We can and should support the development of Title II resolution strategies and the promulgation of a regulation or policy statement by the FDIC on the use of Title II;
- We can and should support central clearing of third-party derivatives and moving as many derivative transactions to exchanges as feasible;
- And we can and should support the development and use of the benchmark portfolio concept to increase transparency.

I have left huge and important issues on the table, including capital levels and their first cousin stress tests, dealing with the so-called "shadow banking system", activity limitations such as the Volcker Rule, extra-territorial application of US rules, liquidity requirements, compliance issues and more – not to mention a whole range other Dodd-Frank issues, of which consumer protection, push-out and the Durbin Amendment are only a few examples. It is good that you have so many experienced and talented presenters and panel members here today to enlighten all of us on these issues.

Thank you.