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September 14, 2018

Ms. Ann E. Misback, Secretary
Board of Governors of the
Federal Reserve System
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Washington, D.C. 20551
Telefacsimile: 202-452-3819
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Mr. Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW
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comments@fdic.gov

Re: Docket No. OP-1614; Proposed 165(d) Guidance for the Domestic Firms;
Resolution Planning Guidance for Eight Large, Complex U.S. Banking Organizations
83 Fed. Reg. 32856 (July 16, 2018) ("Proposed Guidance")
**Second Comment Letter**

Ladies and Gentlemen:

This is my second comment letter in this docket. In Question 1 of the Proposed Guidance, you ask "what key vulnerabilities are not captured?" The QFC stay rules provide that adherents to the ISDA Protocol may be granted certain "creditor protections" that include administrative priority in bankruptcy for guaranty claims on untransferred QFCs, which the GSIB is to seek from the bankruptcy court.[1]

Administrative claims take priority over unsecured and, in some cases, secured claims. Until administrative claims are paid in full, unsecured creditors take $0.[2] There were $45.4 billion in derivatives contracts claims in the Lehman bankruptcy.[3] One GSIB has noted that the contemplated bankruptcy court order would elevate a guaranty claim status in bankruptcy to above the parent's unsecured bondholders.

The risk that up to tens of billions of dollars in ISDA Protocol-adhering counterparty untransferred QFC claims must be paid in full before bondholders are paid anything in a GSIB's bankruptcy is material to that GSIB's bondholders. One GSIB may be an ISDA Protocol-adhering QFC counterparty to another GSIB.

Therefore, two key vulnerabilities not captured are the actions GSIBs must take to avoid immediate civil liability to bondholders on account of agreeing to seek this purported claim subordination, and future liability for implementing it. The risk of subordination is a material

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[1] ISDA Protocol §2. ISDA, *Frequently Asked Questions, ISDA 2018 U.S. Resolution Stay Protocol*, p. 22 (Jul. 2018) ("if the counterparty benefits from a credit enhancement provided by a covered affiliate and the covered affiliate enters proceedings under Chapter 11 of the U.S. Bankruptcy Code, Section 2 of the ISDA Protocol would require either that the counterparty's claim under the credit enhancement be elevated to administrative priority status or be transferred ... within 48 hours"). See also 82 Fed. Reg. 56656 fn. 154; 81 Fed. Reg. 55394 fn. 62; 81 Fed. Reg. 29182 fn. 119.

[2] 11 U.S.C. §507(a). The Bankruptcy Code does not provide for the ranking of administrative claims as purported in the part (a) of definition of Creditor Protection Order in the ISDA Protocol.

[3] Kimberly Summe, *An Examination of Lehman Brothers Derivatives Portfolio Bankruptcy; Would Dodd-Frank Have Made a Difference*, in S. Taylor, Bankruptcy Not Bailout: A Special Chapter 14 (2012). p. 94.

fact concerning the bonds, disclosable under Section 10(b) of the Securities Act of 1933 by nonexempt GSIB issuers. A GSIB that is a trustee under an indenture for bonds of a second GSIB could breach express and implied indenture obligations concerning fiduciary duties and conflicts of interest,[4] and risk not meeting obligations to bondholders respecting enforcement on their behalf post-default,[5] by adhering to the ISDA Protocol and agreeing to seek to subordinate the bondholders for whom it serves as indenture trustee to its own QFC guaranty claims.[6]

The probability of a court granting the subordination is relevant to the materiality of the risks the GSIBs should disclose to, and face from, bondholders. One would expect a noticed bankruptcy court hearing in which the holders of the obligations whose claims would be subordinated could argue against it. As the Board noted without refutation, "commenters [to the proposed QFC stay rule] argued that parties cannot by contract alter the U.S. Bankruptcy Code's provisions, such as the administrative priority of a claim in bankruptcy."[7] If parties could do so by contract, it would be a standard term in senior secured loan agreements. The GSIBs would be helped in assessing the materiality of the risks if you either cited law providing that parties by a prepetition contract can obtain administrative priority for what would otherwise be a general unsecured prepetition claim, or stated you did not have any such cite.

In Question 7 of the Proposed Guidance, you ask: "Do the proposed changes relative to the 2016 Guidance provide sufficient clarity or are additional clarifications required?" I recommend that you provide the clarifications requested above, as well as the following additional clarifications.

First, an administrative claim priority, if granted, would not only subordinate bondholders; it would also subordinate all other unsecured claimants, including depositors. This could have a material impact to a GSIB's resolution plan and communications plan. Please give GSIBs guidance on this.

Second, if senior secured creditors of GSIBs come to believe that they can be subordinated in bankruptcy court by ISDA Protocol-adhering QFC counterparties, they will very likely seek to address it in their loan agreements, by themselves also contracting for a promise to seek administrative priority; perhaps you have a view on the relative priorities of these two sets of creditors competing by contract for administrative priority.

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[4] Conflict of interest provisions are nonwaivable in the case of a nonexempt issuer (§§310(b) and 327 of the Trust Indenture Act of 1939).

[5] E.g., the prudent person enforcement standard of Trust Indenture Act §315(c) for nonexempt GSIB entities, and National Association of Bond Lawyers, Model Form of Trust Indenture, §8.01(d). See, e.g., Schwartz & Sergl, *Bond Defaults and the Dilemma of the Indenture Trustee*, 59 Ala. L. Rev. 1037 (2007).

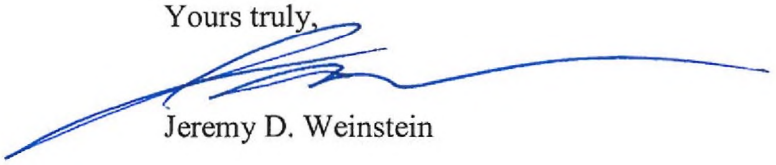
[6] This would also seem to contravene the core purpose of the Trust Indenture Act of 1939, which among other things responded to abuses by indenture trustees taking liens on issuer assets that primed bondholders in violation of the issuer's covenants. See, e.g., Note, *The Trust Indenture Act of 1939: Limitations of the Trustee's Privilege of Lending to the Obligor*, 7 Univ. Chicago L. Rev. 523 (1940); Note, *Restrictive Covenants in Debentures: The Insull Case*, 49 Harv. L. Rev. 620 (1936). See also FDIC, Trust Examination Manual, §6.D., avail. at https://www.fdic.gov/regulations/examinations/trustmanual/section_6/section_vi.html#d_compliance_with_the_trust_indenture_act_of_1939

[7] 82 Fed. Reg. 42903 col. 1. I was such a commenter.

Third, if you believe agreeing to seek administrative priority prepetition is appropriate for a GSIB, even if the administrative priority is unlikely to be granted because there is no legal support for a court to grant it, would Wells Fargo, Bank of America, and their fellow GSIBs providing senior secured loans, or home mortgages, be imprudent not to demand their borrowers agree to seek administrative priority for their prepetition debt to the GSIB?

Fourth, as an individual with cash in excess of insurance in my account at a GSIB, I would like to know if my recovery will be reduced due to administrative priority granted to ISDA Protocol-adhering untransferred QFC counterparties.

Yours truly,



Jeremy D. Weinstein

cc: Mr. Jay Clayton, Chairman, Securities and Exchange Commission
Congressman Mark DeSaulnier
Financial Times