



BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, DC 20551

October 1, 2020

Ms. Rebecca J. Simmons
Sullivan & Cromwell LLP
125 Broad Street
New York, New York 10004

Dear Ms. Simmons:

This responds to your letters submitted on behalf of JPMorgan Chase & Co. (JPMC), New York, New York, and addressed to the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (Board), and the Federal Deposit Insurance Corporation (FDIC) (collectively, the “agencies”), dated July 16, 2018, and November 27, 2019. Your letters request an exemption under each of the agencies’ respective qualified financial contract stay rule (collectively, the “QFC Stay Rule”)¹ for certain custody services contracts. Specifically, from the Board, you request an exemption for the custody services contracts from the requirements of 12 CFR 252.83 and 252.84 of the Board’s QFC Stay Rule.² These contracts involve QFCs subject to the Board’s QFC Stay Rule solely due to the provision of short-term settlement advances, and each party to the covered QFC (other than the covered entity) is a counterparty that is not a covered entity or an excluded bank.³

Pursuant to section 165 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), the Board has established restrictions on the QFCs of U.S. global systemically important bank holding companies (U.S. GSIBs) and the U.S. operations of foreign global systemically important banking organizations (foreign GSIBs). In general, the Board’s QFC Stay Rule requires U.S. GSIBs, companies controlled by a U.S. GSIB (subsidiaries), and the U.S. operations of foreign GSIBs (together, “covered entities”) to amend

¹ 12 CFR part 47 (OCC); 12 CFR part 252, subpart I (Board); and 12 CFR part 382 (FDIC).

² The Secretary of the Board, acting under delegated authority, had granted the firm’s request for temporary extensions of time until October 1, 2020, with respect to the contracts that are the subject of this request.

³ The terms “covered entity” and “excluded bank” have the same meaning as in 12 CFR 252.82(b) and 252.81, respectively.

their derivatives, securities financing transactions, and certain other QFCs (together, “covered QFCs”) in two respects. First, the QFC Stay Rule requires that covered QFCs opt the counterparty into the stay-and-transfer treatment of the Federal Deposit Insurance Act and Title II of the Dodd-Frank Act (U.S. special resolution regimes) to reduce the risk that a counterparty to a QFC governed by non-U.S. law would challenge the applicability of the U.S. special resolution regimes to the QFC.⁴ Second, the QFC Stay Rule requires a QFC to prohibit the counterparty from exercising any cross-default rights (i.e., default rights based on the entry into resolution of an affiliate of the covered entity) unless a creditor protection condition permitted under the QFC Stay Rule (e.g., failure to perform under the contract) is met. Among other things, this requirement is intended to facilitate a single-point-of-entry resolution.⁵

As a U.S. GSIB, JPMC and its subsidiaries are subject to the QFC Stay Rule. The firm indicates that it or its affiliates enter into contracts with clients to provide custodial services such as safekeeping, settlement, asset servicing, and reporting and income services (custody services contracts). These contracts permit the firm or its affiliate to provide short-term settlement advances in connection with the processing of client securities or payment transactions.

In the letters to the agencies, JPMC has requested relief from the requirements of sections 252.83 and 252.84 of the Board’s QFC Stay Rule for custody services contracts that (i) do not include any default right⁶ that could be exercised against a covered entity serving as a custodian or any affiliate of that covered entity and are QFCs subject to the Board’s QFC Stay Rule solely due to the provision of short-term settlement advances; and (ii) comply with the requirements of section 252.84 of the rule, except for certain contractual provisions that would prohibit assignment of the contract without the consent of the client. The requested relief is for custody services contracts entered into by: (1) a foreign subsidiary of the firm (with respect to currently existing and future contracts); (2) a foreign branch of the firm (with respect to currently existing and future contracts); and (3) the firm itself or a U.S. subsidiary of the firm (with respect to currently existing contracts only).

Pursuant to section 252.88(d) of the Board’s QFC Stay Rule, the Board may exempt by order a covered entity from conforming one or more contracts or types of contract to one or more of the requirements of the rule after considering (1) the potential impact of the exemption on the ability of the covered entity, or affiliates of the covered entity, to be resolved in

⁴ 12 CFR 252.83(b). A covered QFC that meets both of the following requirements is not required to be conformed to the provisions of section 252.83(b) of the QFC Stay Rule: (1) the covered QFC states that it is governed by the laws of the United States or a state of the United States; and (2) the QFC counterparty to the covered entity is an individual domiciled in the United States or a company that is incorporated in or organized under the laws of the United States or any state, has its principal place of business located in the United States or any state, or is a U.S. branch or agency. 12 CFR 252.83(a).

⁵ 12 CFR 252.84(b), (f), and (h); see also 12 CFR 252.85(a)–(b).

⁶ “Default right” has the same meaning as in 12 CFR 252.81.

a rapid and orderly manner in the event of the financial distress or failure of the entity; (2) the burden the exemption would relieve; and (3) any other factor the Board deems relevant.⁷

The QFC Stay Rule generally requires that QFCs governed by foreign law or entered into with a foreign counterparty include the counterparty's agreement to be subject to the applicable stay-and-transfer provisions of the U.S. special resolution regimes, in an effort to reduce the risk that such counterparty would challenge those provisions. However, a foreign subsidiary of a U.S. GSIB could not be placed directly into a proceeding under one of the U.S. special resolution regimes, and U.S. law would not prevent the exercise of default rights in the QFCs described below against the foreign subsidiary of a U.S. GSIB. Therefore, exempting QFCs that would not be subject to the stay-and-transfer treatment of the U.S. special resolution regimes would not appear to impact the ability of a U.S. GSIB to be resolved in an orderly manner. In particular, a contract that would not be subject to the stay-and-transfer treatment of the U.S. special resolution regimes (non-U.S., non-linked contracts) meets all of the following criteria: (i) no party to the QFC (other than a foreign subsidiary⁸ of JPMC) is a covered entity or excluded bank; (ii) the QFC is not guaranteed or otherwise supported⁹ by an affiliate¹⁰ of that foreign subsidiary that could itself be placed into one of the U.S. special resolution regimes;¹¹ (iii) the QFC is not linked¹² to an affiliate of that foreign subsidiary; and (iv) the QFC contains no default rights that could be exercised against any other covered entity or excluded bank that itself could be placed into one of the U.S. special resolution regimes. Further, the vast majority of QFCs entered into between material entities of the U.S. GSIBs (including foreign subsidiaries) already have been conformed to the rule's requirements through adherence to the universal protocol and will continue to be subject to the rule's requirements.¹³

With respect to burden, you have represented that there are a significant number of unconformed non-U.S., non-linked contracts and that conforming these contracts to the requirements of the Board's QFC Stay Rule would entail significant time and expense.

⁷ 12 CFR 252.88(d).

⁸ For purposes of this definition, "foreign subsidiary" means a company subject to the Board's QFC Stay Rule that (i) is not incorporated in or organized under the laws of the United States or any state; (ii) does not have its principal place of business located in the United States, including any state; and (iii) is not a U.S. branch or U.S. agency. The terms "state," "U.S. branch," and "U.S. agency" have the same meanings as in 12 CFR 252.2.

⁹ "Support" has the same meaning as in 12 CFR 380.12(b)(3).

¹⁰ "Affiliate" has the same meaning as in 12 CFR 252.2.

¹¹ "U.S. special resolution regimes" has the same meaning as in 12 CFR 252.81.

¹² "Linked" has the same meaning as in 12 CFR 380.12(b)(1). The term "specified financial condition clause" referenced in this definition has the same meaning as in 12 CFR 380.12(b)(2).

¹³ 12 CFR 252.85(a). "Universal protocol" is defined at 12 CFR 252.85(a)(3)(i). The conformed QFCs between U.S. GSIB entities represent over 95 percent of the notional value of derivatives of the firms and a significant portion of other QFCs, including those most concerning from an interconnectedness perspective.

Specifically, the firm indicates that it would experience considerable burden in educating counterparties regarding the requirements of the rule, negotiating amendments to the relevant contracts, and executing and reviewing such amendments.¹⁴

For these reasons, an exemption for non-U.S., non-linked contracts appears to be appropriate. However, with respect to custody services contracts that are not non-U.S., non-linked contracts, the requested exemption may impact the ability of the firm to be resolved in a rapid and orderly manner in the event of the financial distress or failure of the entity. These contracts would fall within the FDIC's authority as receiver of a covered entity placed into a proceeding under one of the U.S. special resolution regimes. As a result, exempting these contracts from the requirements of sections 252.83 and 252.84 of the Board's QFC Stay Rule could impact the ability of the covered entity or its affiliates to be resolved in a rapid and orderly manner.

Accordingly, the Board has granted JPMC an exemption for non-U.S., non-linked custody service contracts that meet the criteria described on page three of this letter from the requirements of 12 CFR 252.83 and 252.84 and has denied the request for an exemption for custody services contracts that are not non-U.S., non-linked contracts.¹⁵ In addition, for those custody service contracts for which the requested relief has been denied, the Secretary of the Board, acting under delegated authority, has granted the firm a period of six months from the date of this letter to conform the QFCs to the requirements of the Board's QFC Stay Rule.¹⁶

This action may be revised or revoked, based on changes to applicable regulations or other relevant factors. This action is based on all the facts of record, including the information discussed above, and the representations in your submissions and supplemental information. Any material change in those facts or representations could affect this approval and should be communicated promptly to Board staff.

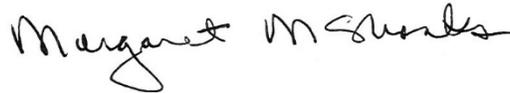
¹⁴ In considering your request, the Board also has taken into account the covered entity that has entered into the custody services contract. 12 CFR 252.88(d)(3).

¹⁵ In considering this request, Board staff consulted with staff of the OCC and FDIC in an effort to maintain consistent interpretations under the QFC Stay Rule.

¹⁶ 12 CFR 265.5(a)(2).

Please contact Lucy Chang at (202) 475-6331 or Evan Hechtman at (202) 263-4810, both of the Board's Legal Division, or Lesley Chao at (202) 974-7063 or Rebecca Alper at (202) 475-6321, both of the Board's Division of Supervision and Regulation, if you have any questions.

Very truly yours,

A handwritten signature in black ink that reads "Margaret McCloskey Shanks". The signature is written in a cursive style with a large initial "M" and a long, sweeping underline.

Margaret McCloskey Shanks
Deputy Secretary of the Board

cc: Office of the Comptroller of the Currency
Federal Deposit Insurance Corporation
Lauren A. Anderson, The Bank Policy Institute