

Comptroller of the Currency Cites TBTF Risks at Large Regional Banks

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On April 1, Acting Comptroller of the Currency Michael J. Hsu stated that the OCC, under the “significant role” it plays in national bank mergers, is considering certain “resolvability safeguards” with its review of larger bank merger transactions. He expressed concern about a gap in the resolvability expectations of the eight U.S. global systemically important banks (GSIBs) and the largest non-GSIBs, what he calls “large regionals.” Hsu suggested that this gap may present a new too big to fail (TBTF) risk and indicated that new standards for the potential failure of large regionals may be on the horizon.

According to Hsu, the traditional purchase and assumption (P&A) transactions with FDIC loss-share provisions, if used by GSIBs to acquire failed large regionals, would result in “shotgun marriages” with multiple drawbacks, including:

- GSIBs would be made “significantly more systemic”;
- GSIBs would only be able to conduct minimal due diligence;
- There would be limited identification of integration challenges; and
- Trust in the process, and the government’s involvement, would likely erode.

As an alternative, Hsu advocated for a broader, long-term perspective on financial stability and a related approach to resolution of any large regional bank failures in the future. In his view, a deviation from the current tailoring of prudential standards is warranted, particularly given the growth in the size and number of large regionals.

While acknowledging that large regionals “are not nearly as complex or global as the GSIBs,” Hsu indicated that if certain requirements from the prudential standards that apply to GSIBs were applied to large regionals, then large regionals would be more resolvable and TBTF risk may be minimized. Specifically, Hsu advocated for the following resolvability requirements to be made applicable to large regionals:

1. **Single-point-of-entry resolution strategy.** In this type of resolution, only the parent holding company would file for bankruptcy or be placed into receivership, allowing subsidiaries to continue operation and avoid the complications of multiple proceedings.

2. **Total loss absorbing capital requirement (TLAC).** This would require large regionals to hold a minimum amount of long-term debt at the parent level, resulting in private investors absorbing losses rather than taxpayers funding a bailout.
3. **Separability.** Require large regionals to structure and operate certain lines of business and/or large portfolios so that they can be sold quickly, providing an avenue to break up a large regional relatively quickly.

The changes advocated by Hsu would likely require congressional action, not to mention concurrence by the FDIC and Federal Reserve. Nevertheless, Hsu suggested the OCC could play a role by conditioning approval of large national bank mergers on the implementation of single-point of-entry resolution strategies, TLAC requirements, and separability.

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