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Transcript of FDIC Board of Directors meeting, closed session

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UNITED STATES OF AMERICA
FEDERAL DEPOSIT INSURANCE CORPORATION

+ + + + +

BOARD OF DIRECTORS

+ + + + +

MEETING

+ + + + +

CLOSED SESSION

+ + + + +

SUNDAY,

NOVEMBER 23, 2008

+ + + + +

The Board convened via telephone,
SHEILA C. BAIR, Chairman, presiding.

PRESENT:

SHEILA C. BAIR, Chairman
MARTIN J. GRUENBERG, Vice Chairman
THOMAS J. CURRY, Director
JOHN C. DUGAN, Director (Comptroller of
the Currency)
JOHN M. REICH, Director (Office of Thrift
Supervision)

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C-O-N-T-E-N-T-S

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1 P R O C E E D I N G S

2 CHAIRMAN BAIR: Hello, who do we
3 have?

4 MR. Feldman: Chairman Bair, this is
5 Bob Feldman. We have Vice Chairman Gruenberg
6 at the Board table, and on the line we have
7 Director Curry, Director Dugan and Director
8 Reich.

9 CHAIRMAN BAIR: Okay, great. Are we
10 all set? All the staff there?

11 MR. Feldman: And we have staff here
12 as well.

13 SUNSHINE MOTION

14 CHAIRMAN BAIR: Okay, great, let's
15 call the meeting to order, then.

16 May I have a Sunshine motion,
17 please?

18 VICE CHAIRMAN GRUENBERG: I move.

19 CHAIRMAN BAIR: May I have a second?
20 I'll second. All in favor say aye.

21 (Chorus of ayes)

22 CHAIRMAN BAIR: The motion is agreed

1 to, thank you.

2 No summary agenda and one item on
3 the discussion agenda. It's a memorandum and
4 resolution relating to Citibank, National
5 Association, Las Vegas, Nevada, and its
6 affiliated insured depository institution.

7 John Corston, Jim Wigand, and John
8 Thomas will present the case.

9 MEMORANDUM AND RESOLUTION RELATING TO
10 CITIBANK NATIONAL ASSOCIATION

11 MR. WIGAND: Yes, good evening,
12 Madam Chairman, and members of the board.

13 Staff recommends that the Board
14 find that the failure of Citigroup, Inc., and
15 its insured affiliate banks and thrifts would
16 have serious adverse effects on domestic and
17 international economic conditions and
18 financial stability.

19 Citigroup's failure would seriously
20 and negatively affect already disrupted credit
21 markets including short term inter-bank
22 lending, counterparty relationships and QFC

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1 markets, and bank and senior subordinated debt
2 markets, and would further disrupt the related
3 markets in derivative products and other
4 markets.

5 In addition it would have serious
6 consequences to the functioning of the global
7 payment system.

8 It is recommended that the Board
9 make a systemic risk determination and
10 authorize staff to take steps necessary as
11 outlined below, and I will describe these
12 momentarily.

13 Based on preliminary information,
14 staff estimates there will be no loss to the
15 deposit insurance fund or a need for a special
16 assessment.

17 In order to prevent the foregoing
18 systemic risk, staff recommends that the Board
19 authorize the FDIC to enter into a transaction
20 to provide for shared loss coverage on a
21 designated pool of assets up to \$306 billion.

22 The FDIC and the U.S. Treasury's

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1 Troubled Asset Relief Program will provide
2 guarantees on certain residential assets for
3 10 years and certain other assets for a period
4 of five years.

5 The FDIC will be exposed to loss
6 only after Citigroup absorbs the first \$37
7 billion in losses and the Treasury absorbs the
8 next \$5 billion in losses.

9 The FDIC's loss will be capped at
10 about \$10 billion, and will receive
11 compensation in the form of \$3 billion in
12 preferred shares for providing this guarantee.

13 In addition, the Board of Governors
14 of the Federal Reserve will provide certain
15 financing secured in part by the assets in the
16 portfolio of consumer and commercial and real
17 estate loans designated by the agencies and
18 Citigroup.

19 Citigroup will manage the assets
20 with instructions provided by the FDIC, the
21 U.S. Treasury, and the Federal Reserve.
22 Instructions will include the required use of

1 loan modification procedures comparable to
2 those that are currently being employed at
3 IndyMac Federal Bank, unless otherwise agreed
4 to by the FDIC.

5 In addition, Citigroup will be
6 subject to specific limitations on executive
7 compensation and dividends during the loss
8 share period.

9 The FDIC, OCC, and OTS have
10 determined that the insured entities meet the
11 requirements under section 13(c)(8) of the
12 Federal Deposit Insurance Act for receiving
13 direct financial assistance before the
14 appointment of a receiver, specifically, that
15 the institution's management has been
16 competent, and has complied with applicable
17 laws, rules, and supervisory directives and
18 orders; and two, that the institutions and its
19 management did not engage in any insider
20 dealing, speculative practice or other abusive
21 activity.

22 Additionally the assistance

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1 provided will increase existing capital
2 levels, and it is unlikely that the
3 institution can make currently applicable
4 capital standards going forward without this
5 assistance.

6 In exchange for the guarantees I've
7 just discussed, Citigroup has agreed to seek
8 the prior approval of the agencies before
9 paying dividends for two years; develop a
10 long-term executive compensation program that
11 rewards long-term performance and
12 profitability that needs to be approved by the
13 agencies; and that they seek the agencies'
14 prior approval associated with the award of
15 this program.

16 Additionally, as I indicated
17 before, they have to agree to implementing a
18 loan modification program.

19 CHAIRMAN BAIR: That we've approved.

20 I think that the language got changed,
21 actually, since the Board case was written.
22 It would have to be an FDIC-approved loan

1 modification protocol.

2 MR. WIGAND: With that I'm going to
3 turn it over to John Corston, who will provide
4 a supervisory history for the institution.

5 MR. Corston: Thank you.

6 Citibank, N.A., is a nationally
7 chartered bank founded in 1812. It's the lead
8 bank within Citigroup, a financial holding
9 company regulated by the Federal Reserve.

10 Citibank is the third largest bank
11 in the nation and is the predominant legal
12 entity, representing 63 percent of the
13 consolidated holding company assets.

14 The insured legal entities of
15 Citigroup consist of three national banks, one
16 Federal savings bank, and one state nonmember
17 bank. With the exception of the composite
18 "3"-rated lead bank, the others are rated
19 composite "2".

20 Citigroup is the largest consumer
21 finance lender in the world, third largest
22 mortgage servicer, and fourth largest student

1 lender. It is the world's largest credit card
2 lender, and the third largest in the United
3 States.

4 It is also one of the world's
5 largest private banking and private wealth
6 management businesses.

7 The risk profile of Citibank is
8 increasing rapidly due to the market's lack of
9 confidence in the company and the
10 substantially weakened liquidity position.

11 On Friday, November 21st, the
12 United Kingdom's Financial Services Agency
13 imposed a \$6.4 billion cash lockup requirement
14 to protect the interests of the UK broker-
15 dealer. That day, market acceptance of
16 Citibank's liabilities diminished as the
17 company's stock plunged to a 16-year low.
18 Credit default swap spreads widened 75 basis
19 points to 512, and counterparties advise that
20 they would require greater collateralization
21 on any transactions with Citibank.

22 Without substantial government

1 intervention that results in a positive market
2 perception on Monday morning, the OCC and
3 Citigroup project that Citibank will be unable
4 to pay obligations or meet expected deposit
5 outflows next week.

6 Citigroup's contractual cash flow
7 projections show that a total of 7.2 percent
8 deposit runoff will result in no cash surplus.

9 Current requests by Citigroup to
10 the Federal Reserve to expand the Commercial
11 Paper Funding Facility and to expand
12 collateral and entities eligible for posting
13 to the Primary Dealer Credit Facility and the
14 Term Securities Lending Facility would provide
15 short-term funding relief.

16 However, the additional funding
17 provided by these programs would not be
18 sufficient to withstand the extensive deposit
19 runoff.

20 Regarding systemic risk, it appears
21 likely that any transaction implemented by the
22 FDIC under a least-cost framework would have

1 significant adverse effects on economic
2 conditions and the financial markets, based on
3 Citigroup's size and the markets in which it
4 operates.

5 Given Citigroup's significant
6 international presence, effects on money
7 market liquidity could be expected on a global
8 basis. Term funding markets remained under
9 considerable stress.

10 These pressures have increased over
11 the past week with a loss of investor
12 confidence in financial institutions'
13 performance, as evidenced by a significant
14 drop in bank equity values, and another round
15 of increase in banks' credit default swap
16 spreads.

17 Citigroup has been particularly
18 vulnerable with its exposure to credit and
19 market losses, coupled with its dependence on
20 international operations for funding.

21 The imposition of a least-cost
22 resolution on Citigroup would likely have

1 major systemic effects. Both financial
2 stability and overall economic conditions
3 would adversely be affected for the reasons
4 that I just discussed.

5 In view of the current intense
6 financial strains, as well as the likely
7 consequences to the general economy and
8 financial system of a least-cost resolution of
9 the third largest commercial bank in the
10 United States, staff believes that
11 circumstances are such that invocation of a
12 systemic risk exception is justified.

13 With that we can turn it over to -

14 MR. WIGAND: Now, with that, if
15 there are any questions, we'll be happy to
16 answer them.

17 CHAIRMAN BAIR: Okay, thank you.

18 MR. THOMAS: If I may, one further
19 note. There was discussion of least cost.
20 The actual problem is not that this is a
21 least-cost resolution. The expected cost is
22 zero. The problem is it's open bank

1 assistance.

2 CHAIRMAN BAIR: Right, that we're
3 supporting shareholders, that's right. Thank
4 you, John, that's a good clarification.

5 Vice Chairman Gruenberg.

6 VICE CHAIRMAN GRUENBERG: Thank you,
7 Madam Chairman. I'm prepared to support this
8 case. I think the finding of systemic risk is
9 clear and justified.

10 I think it also suggests the
11 exceptional cooperative effort among the
12 Federal bank regulatory agencies - the
13 Treasury, the Federal Reserve, as well as the
14 FDIC, and their commitment to do what is
15 necessary to maintain financial stability in
16 what are clearly an extraordinary set of
17 market conditions.

18 And I would add that the
19 conditionality imposed on the institution in
20 this case relating to dividends and executive
21 compensation and loan modifications, I view as
22 essential, an essential part of this case.

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1 Thank you very much.

2 CHAIRMAN BAIR: Okay, thank you.

3 Director Curry.

4 DIRECTOR CURRY: I echo the comments
5 of the Vice Chairman. I think that the case
6 is amply made that the systemic risk
7 determination standard has been met, and I
8 hope that this particular open bank assistance
9 is sufficient for this institution, and that's
10 - that I'm prepared to vote in favor of this
11 application or transaction.

12 CHAIRMAN BAIR: Okay, thank you.

13 Director Dugan.

14 DIRECTOR DUGAN: Thank you, Madam
15 Chairman. I strongly support this case. I
16 think it's, as others have said, amply
17 justified by the facts. It is about
18 confidence, not just in this institution, but
19 in other banks as well. And I think it's
20 absolutely critical that we act decisively to
21 take measures to address the situation.

22 I hope this is adequate to do the

1 job, and I think, with the combination of
2 resources from all the agencies and the
3 Treasury Department, I'm hopeful that it will
4 be, and I think we need to go forward with it.

5 So again, I strongly support it.

6 CHAIRMAN BAIR: I assume - does OCC
7 have a supervisory strategy for helping get
8 the situation under control again?

9 DIRECTOR DUGAN: Well, this is all
10 about confidence right now, not about the
11 capital in the company or its reserve level,
12 and we'll be closely monitoring the situation
13 and dealing with issues related to
14 supervision.

15 But the issue now is the potential
16 of a large world-wide bank run, and that's
17 what's got to be brought under control.

18 CHAIRMAN BAIR: Well, I certainly
19 agree, and that's why we're doing this. But I
20 think we'll look forward to working with you
21 in terms of your supervisory strategy, and I
22 know we are all committed to making sure Citi

1 pursues all strategic options including
2 selling itself or selling pieces of itself.
3 This is not the first time this institution
4 has become challenged.

5 I understand that there is a
6 significant off-balance-sheet exposure that
7 could be having to come on book at the end of
8 next year which could further complicate the
9 situation. So we're obviously deeply in here
10 with the 77 billion in unsecured senior debt
11 guarantees, maybe more if they came in to
12 apply for an increase over the 125 percent
13 gap. And the government's obviously very
14 deeply on the hook now. And we are providing
15 additional reinsurance on the losses on this
16 loan portfolio. So it certainly is something
17 that we need to do. But I think it's not
18 going to be enough. I think this institution
19 has some significant problems and it's going
20 to require a very aggressive supervisory
21 strategy or we are going to be back in writing
22 some more checks.

1 Director Reich, do you have any
2 comments or questions?

3 DIRECTOR REICH: Well, actually I
4 do. I have a number of questions. I probably
5 had the least involvement with this, so bear
6 with me while I do ask a few questions.

7 I am going to be supportive of
8 this. It's obviously a systemic risk
9 situation. I don't have any question about
10 that.

11 But because of my lack of
12 involvement with the discussion over the last
13 few days, I do have some questions. And the
14 first one is . . . pertains to liquidity. I
15 think, in our principals' conference call
16 Friday morning, it was reported that Citi's
17 liquidity was somewhere in the neighborhood of
18 - I don't recall the exact number - but \$150
19 billion or \$160 billion, or somewhere in that
20 vicinity. Is there a current - a more current
21 number on what we think their liquidity is, or
22 access to liquidity?

1 CHAIRMAN BAIR: John, go ahead.

2 DIRECTOR DUGAN: Last I heard, it
3 had declined about 130, but I don't have the
4 most recent information.

5 DIRECTOR REICH: Had declined to
6 130?

7 DIRECTOR DUGAN: Yeah, that was the
8 most - that's the last I heard.

9 DIRECTOR REICH: Okay. How about
10 the asset quality rating? I think that the
11 case indicates that at the last most recent
12 examination the asset quality was a "2". Do
13 we still think it's a "2" and the composite a
14 "3"?

15 DIRECTOR DUGAN: Doug Roeder, are
16 you on?

17 MR. ROEDER: Yeah, John.

18 DIRECTOR DUGAN: Maybe you could
19 address that question.

20 MR. ROEDER: Yeah, in terms of the
21 asset quality we've been looking at that in
22 terms of a downgrade. Obviously, the

1 portfolios are not getting better; they are
2 getting worse. So I would say that was
3 subject to a potential downgrade, maybe
4 downgradeable very shortly.

5 Second, in terms of the composite
6 we had it as a "3". Obviously their liquidity
7 situation rapidly changed, so - but with the
8 fix - I'm not in a position to necessarily say
9 that that is anything less than a "3", given
10 the other conditions and the support from this
11 transaction.

12 CHAIRMAN BAIR: How can you say
13 that? I mean we were on the verge of having
14 to close this institution because it can't
15 meet its liquidity Monday morning. How can
16 you keep liquidity at a "3". They've got 500
17 billion in foreign deposits that nobody can
18 guarantee. How can you keep it at a "3"? I
19 don't understand that.

20 DIRECTOR DUGAN: I think it has to
21 do with the situation once this thing gets put
22 in place, that's all.

1 MR. ROEDER: Exactly right.

2 CHAIRMAN BAIR: In other words, once
3 a lot of government assistance is injected
4 into this institution, then it stays at a "3".

5 That is not the criteria we use. That is
6 certainly not the criteria we use for other
7 banks. You can't stabilize liquidity without
8 significant government support.

9 So how do you rate a "3"? Is that
10 the standard now that people get a "3" if with
11 government assistance they can have adequate
12 liquidity? That doesn't make any sense to me.

13 DIRECTOR DUGAN: Well, I think it
14 has been the actual standard. If at all in
15 question about what is their liquidity
16 situation at a particular point in time given
17 all the things, they already have a certain
18 amount of government assistance already, and
19 now they have more. And the question is, it's
20 an all-in - if you add in all the factors
21 where are they? And we will adjust and take a
22 look at that situation after we see what

1 happens with this deal by the government.

2 CHAIRMAN BAIR: Well, John, I just
3 think this gets back to my question earlier
4 is, what is your supervisory strategy? And I
5 got to tell you, I don't think this is going
6 to fix Citi. And unless you figure out a way
7 to stabilize that situation, we are going to
8 be back in here writing more checks. So I
9 just want to be on the record saying that, and
10 we want to work with you constructively on it.
11 But I think we all need to be realistic about
12 some of the underlying problems at this
13 institution. It's not just because the market
14 is having problems; this institution has some
15 problems very specific to itself. And so I
16 think we all need to work together on how
17 we're going to fix that.

18 DIRECTOR DUGAN: We will continue to
19 work hard to address the problems of
20 Citigroup. We are not committing to a
21 particular strategy now. We don't know what
22 the situation will be once this gets

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1 addressed, and when it is, we are looking at
2 all kinds of alternatives. And we will keep
3 you posted.

4 DIRECTOR REICH: Well, let me move
5 on to another question. I had a briefing
6 earlier this afternoon, and we talked about
7 ring-fencing 300-plus billion in assets, and
8 I'd like to have a better understanding of
9 what ring-fencing means.

10 MR. THOMAS: I think that shorthand,
11 really - what it means in practice here is
12 that \$306 billion of assets will be very
13 specifically identified. It's not that they
14 can move things in and out after we start
15 this.

16 DIRECTOR REICH: Will they be moved
17 off balance sheet?

18 MR. THOMAS: No, they'll stay on the
19 balance sheet - and Citi will continue to work
20 the assets. But there will be a complete
21 record of what they are from the beginning; no
22 substitution.

1 DIRECTOR REICH: Okay. The terms of
2 guarantee on the draft term sheet, or at least
3 one of the terms - there have been so many - I
4 don't think I printed out the last one which
5 came about three minutes before this meeting -
6 refer to the FDIC's standard loss sharing
7 protocol. What is the FDIC's standard loss-
8 sharing protocol? I've been on the Board for
9 eight years, and I don't know what that is.

10 MR. WIGAND: Well, fortunately, we
11 haven't had to use them very much until
12 recently. Basically what we do is that we
13 have a set of requirements in our loss share
14 agreements with respect to charges for various
15 expenses. For example in our standard loss-
16 sharing protocols, as we indicate here, Citi
17 is going to have to manage a pool of assets.
18 Its internal expenses are not passable back
19 and charged against the loss coverage, unless
20 they are third-party expenses for certain
21 types of charges. For example, certain types
22 of legal fees are chargeable and can be passed

1 through.

2 But most of the expenses of
3 managing and servicing the pool have to be
4 absorbed by the covered entity.

5 Additionally, in this particular
6 agreement, I don't think I was clear about
7 this in the presentation, the losses beyond
8 the \$37 billion are split 90-10 to the
9 appropriate counterparty. So, for the next 5-
10 1/2 billion dollars roughly of losses, the
11 Treasury will take 5 billion of that, and
12 then, for the next approximately \$11 billion
13 of losses, the FDIC will take \$10 billion of
14 that loss bucket. And, beyond that, to the
15 extent there are any losses, then the Federal
16 Reserve Board is going to have to absorb 90
17 percent of those.

18 So that's -

19 DIRECTOR REICH: Ninety percent or
20 100 percent?

21 MR. WIGAND: Ninety percent. The
22 loss share - the 10-90 split continues for the

1 covered pool.

2 DIRECTOR REICH: Okay. And is the
3 first loss for Citi, is it 37 or 42?

4 MR. WIGAND: It's 37 billion for
5 Citi, with the Treasury taking the next five.

6 DIRECTOR REICH: Okay. Dividend
7 policy: the case says the institution is
8 prohibited from paying common stock dividends
9 in excess of a penny a share for three years
10 without Treasury, FDIC, Fed consent. Does the
11 OCC have a voice in that? I didn't see any
12 reference to the OCC.

13 Mr. THOMAS: The OCC has a separate
14 basis on which it can act. This basically is
15 a contractual provision because these are the
16 agencies putting up the money.

17 DIRECTOR REICH: Okay. Are there
18 any changes in management expected or
19 required?

20 CHAIRMAN BAIR: Good question.
21 John, can you address that, John Dugan?

22 DIRECTOR DUGAN: There is no changes

1 in management required by this agreement.

2 CHAIRMAN BAIR: What about your
3 supervisory strategy? Are we looking at the
4 quality of management?

5 DIRECTOR DUGAN: We are always
6 looking at the quality of management. We will
7 see how this goes. You can't just go in and
8 kick people out unless you have other people
9 that are willing and able to step up to do it.
10 But that is something we are evaluating.

11 DIRECTOR REICH: I think that I've
12 asked the questions that I wanted to ask.
13 Obviously, this is a very serious situation;
14 I'm very sympathetic to the situation that
15 Comptroller Dugan is in. There isn't any
16 doubt in my mind that this is a systemic
17 situation.

18 In hindsight, I think there have
19 been some systemic situations prior to this
20 one that were not classified as such. The
21 failure of IndyMac pointed the focus to the
22 next weakest institution, which was WaMu, and

1 its failure pointed to Wachovia, and now we're
2 looking at Citi, and I wonder who's next.

3 I hope that the regulators, all of
4 us, including Treasury and the Fed, are
5 looking at these situations in a balanced
6 manner, and I fear there has been some
7 selective creativity exercised in the
8 determination of what's systemic and what's
9 not and what's possible for the government to
10 do, and what's not.

11 There has been a high degree of
12 pressure exerted in certain situations, and
13 not in others, and I'm concerned about parity.

14 Having said that, I do support this
15 case, and I'm prepared to vote.

16 CHAIRMAN BAIR: Okay, great. May I
17 have a motion with respect to Citibank, N.A.,
18 Las Vegas, Nevada and its related insured
19 depository institutions?

20 VICE CHAIRMAN GRUENBERG: I move,
21 Madam Chairman. Before we vote, I'm sitting
22 here in the board room with a room full of

1 staff that have been here the whole weekend,
2 and I'd be remiss in not thanking them as well
3 as the staff for the other agencies, for their
4 extraordinary efforts.

5 CHAIRMAN BAIR: I think you are
6 absolutely right, and many of them still have
7 a long night ahead of them in terms of getting
8 this executed and dealing with the press and
9 the overseas operations. So thanks to you,
10 Vice Chairman Gruenberg, for braving and being
11 in the office. Good for you.

12 So, yes, as always, thanks to all
13 our wonderful staff, and again, above and
14 beyond the call of duty in getting this put
15 together in a very tight timeframe.

16 So I had a motion?

17 VICE CHAIRMAN GRUENBERG: I move.

18 CHAIRMAN BAIR: May I have a second
19 please?

20 DIRECTOR CURRY: Second.

21 CHAIRMAN BAIR: All in favor say
22 aye.

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(Chorus of ayes)

CHAIRMAN BAIR: Aye. The motion is agreed to. Thank you very much. That concludes the discussion agenda.

Any other business before we adjourn?

Okay, great, the meeting is adjourned. Thank you very much.

(Whereupon the meeting was adjourned.)