11-23-2008

Memo to the FDIC Board from James R. Wigand and Herbert J. Held re recommendation for systemic risk determination for Citigroup

James R. Wigand

Herbert J. Held

November 23, 2008

MEMORANDUM:	The Board of Directors
THROUGH:	Mitchell L. Glassman, Director Mitchell L. Glassman Division of Resolutions and Receiverships
	Sandra L. Thompson, Director Division of Supervision and Consumer Protection
FROM:	James R. Wigand, Deputy Director Franchise and Asset Marketing Branch Division of Resolutions and Receiverships
	Herbert J. Held, Assistant Director Franchise and Asset Marketing Branch Division of Resolutions and Receiverships
SUBJECT:	Citibank, National Association, Las Vegas, Nevada Citibank (South Dakota), National Association, Sioux Falls, South Dakota Department Stores National Bank, Sioux Falls, South Dakota Citicorp Trust Bank, FSB, Wilmington, Delaware Citibank (Banamex USA), Century City, California
	Citigroup Inc. (Bank Holding Company) Information ($ Thousands) (As of June 30, 2008): Total Assets: $2,100,385,000 Total Deposits (including Foreign): $803,642,000 Uninsured Deposits: $181,183,775, Foreign Deposits: $543,287,000 Tier 1 Leverage/Total Risk Based (Lead Bank): 6.51/13.38
	UFIR Rating (Lead Bank): 2-2-3-3-3-3/3 (4/18/2008)

Recommendation

Staff recommends that the Board find that the failure of Citigroup, Inc. and its insured affiliate banks and thrifts would have serious adverse effects on domestic and international economic conditions and financial stability. Citigroup's failure would seriously and negatively affect already disrupted credit markets, including short-term interbank lending, counterparty relationships in

Qualified Financial Contract markets, and bank senior and subordinated debt markets and would further disrupt the related markets in derivative products and other markets. It is recommended that the Board make a systemic risk determination and authorize staff to take steps necessary steps, as outlined below. Based on preliminary information, staff estimates no loss to the Deposit Insurance Fund.

In order to prevent the foregoing systemic risks, staff recommends that the Board authorize the FDIC to enter into a transaction to provide for shared loss coverage, along with the U.S. Treasury's Troubled Asset Relief Program, with the FDIC's potential loss protected by the issuance of preferred stock by Citigroup. The FDIC and the U.S. Treasury's Troubled Asset Relief Program (US/TARP) will provide guarantees on certain residential assets for 10 years and certain other assets for a period of 5 years. The FDIC will be exposed to loss only after Citigroup absorbs the first $37 billion in losses and the TARP absorbs $5 billion in losses. The FDIC's loss share will be capped at $10 billion and it will receive compensation in the form of $3 billion in preferred stock. In addition, the Board of Governors of Federal Reserve will provide certain financing secured, in part, by assets in a portfolio of consumer and commercial loans designated by the Agencies and Citigroup.[1] The chart below provides detail on estimated losses.

[1] The FDIC, Treasury and the Board of Governors of Federal Reserve will be referred to collectively as the Agencies.

Ring Fenced Portfolio	Original Value	Current Value	LLR	Mark	Current Price	Examiner Judgment Base	Stress
ACCRUAL ASSETS							
Citi Home Mortgages	**153**	**153**	**6.3**			**11.8**	**20.0**
Total Seconds	**85**	**85**	**3.1**				
Second Mortgages Funded	60	60	3.1				
Second Mortgages UnFunded	25	25	0.0				
Total Firsts	**68**	**68**	**3.2**				
Alt-A	24	24	0.6				
Subprime	33	33	2.5				
Prime 1st (Wall Street)	11	11	0.2				
Retail Autos	**19.7**	**19.7**	**0.9**			**3.0**	**3.6**
CRE Portfolio (Accrual & MTM)	**39.6**	**37.0**	**0.9**	**2.69**		**6.1**	**7.2**
Lev Loans	**22.1**	**16.3**		**5.83**			
MARK TO MARKET ASSETS	117.2	81.4				0.0	0.0
CDO (ABCP only)	23.4	12.2		11.2	52%		
Big 3 Autos	30.3	29.1		1.3	96%		
ARS	12.0	9.5		2.5	79%		
Alt-A	22.9	14.4		8.8	63%		
Subprime	6.3	2.7		3.6	43%		
Monolines	9.4	4.5		5.0	47%		
ICG Strategic PE	0.7	0.5		0.0	75%		
US SIV	12.4	8.6		3.8	69%		
TOTALS	**352**	**307**	**8.1**	**44.6**		**20.9**	**30.8**

Citigroup and the Agencies will share losses with Citigroup will having a 10 percent loss share on all losses in excess of the $37 billion. The US/TARP takes the second loss position up to $5 billion and the FDIC takes the third loss position up to $10 billion. The loss share of the FDIC and US/TARP will be capped as above. The Federal Reserve will take remaining losses. Citigroup will manage the assets, with instructions provided by the FDIC, US/TARP and Federal Reserve. Instructions will include required use of loan modification procedures comparable to those used at IndyMac Federal Bank, unless otherwise agreed. In addition, Citigroup will be subject to specific limitations on executive compensation and dividends during the loss share period.

The FDIC, OCC, and OTS have determined that the insured entities meet the requirements under Section 13 (c) 8 of the FDI Act for receiving direct financial assistance before the appointment of a receiver. Additionally; assistance will increase existing capital levels and improve liquidity.

Commitments by Citigroup

In exchange for the guarantees discussed above, Citigroup has agreed to 1) seek the prior approval of the Agencies before paying dividends for 2 years; 2) develop an executive compensation program that rewards long-term performance and profitability to be approved by the Agencies; 3) implement loan modification procedures conforming with the FDIC's model used at IndyMac Federal Bank for mortgages in the asset pool unless otherwise agreed. Additionally the FDIC and US/TARP will receive preferred stock as reasonable compensation for the guarantees provided.

Executive Summary

Cititbank, NA (CBNA or Bank) is a nationally chartered bank founded in 1812 that is the lead bank within Citigroup, Inc. (Citigroup) a financial holding company regulated by the Federal Reserve. CBNA is the third largest bank in the nation and is the predominant legal entity representing 63 percent of consolidated holding company assets. The insured legal entities of Citigroup consist of three national banks, one federal savings bank and one state non-member bank. Citigroup is the largest consumer finance lender in the world, third largest mortgage servicer and the fourth largest student lender. It is the world's largest credit card lender and the third largest in the United States. It is also one of the world's largest private banking and private wealth management businesses.

Citigroup has three principal nonbank subsidiaries; Citigroup Global Markets Holdings, Inc (broker-dealer); Citigroup Funding, Inc (primary funding vehicle of Citigroup); and Associates First Capital Corporation (parent company of CitiFinancial , which provides consumer finance). There is one foreign banking subsidiary Grupo Financiero de Banamex SA de CV (Mexican banking organization).

CBNA engages in extensive foreign activities and has operations in over 100 countries. It operates approximately 1,000 retail branches in 13 states, the District of Columbia, and Guam. CBNA reported foreign assets of $612 billion and foreign deposits of $554 billion held either in direct foreign branches of CBNA or in other foreign entities that are mostly owned by the CBNA's Edge Act investment subsidiary, Citibank Overseas Investment Corp. (COIC). COIC has over 20 foreign banks that are headquartered and chartered in countries around the world. The risk profile of CBNA is increasing rapidly due to the market's lack of confidence in the company and a substantially weakened liquidity position. Liquidity has reached crisis proportions, such that the CBNA is projected to be unable to meet its obligations. Most recently, on Friday, November 21, 2008, the UK's Financial Services Agency imposed a $6.4 billion cash lockup requirement to protect the interests of the UK broker dealer.

On Friday November 21, 2008, market acceptance of CBNA's liabilities diminished, as the company's stock plunged to a 16-year low, credit default swap spreads widened by 75 basis points to 512.5 basis points, and counterparties advised that they would require greater collateralization on any transactions with CBNA.

Supervisory History and Condition

Condition

Without substantial government intervention that results in a positive market perception on Monday morning, the OCC and Citigroup project that CBNA will be unable to pay obligations or meet expected deposit outflows next week. Citigroup contractual cash flow projections[2] show that a total of 7.2 percent deposit run off will result in no cash surplus. CBNA management has

[2] The contractual cash flow projection does not include additional haircuts on existing secured finance transactions.

prepared stress scenario estimates that show deposit runoff of approximately 2 percent of total deposits per day.

Current requests by Citigroup to the Federal Reserve to expand the Commercial Paper Funding Facility (CPFF) and to expand collateral and entities eligible for posting to the Primary Dealer Credit Facility (PDCF) and the Term Securities Lending Facility (TSLF) would provide short-term funding relief. However, the additional funding provided by CPFF, PDCF, and TSLF would not be sufficient to withstand extensive deposit runoff. Doubling CPFF capacity would result in a total incremental liquidity of $76.5B; however, a 10.2 percent deposit runoff would eliminate this incremental liquidity.

Expanding collateral and entities eligible at the PDCF will likely replace current secured finance funding and, as a result, would likely not provide significant incremental liquidity or be sufficient to offset substantial deposit runoff. Expanding collateral and entities eligible to pledge at the discount window may provide incremental liquidity. However, the collateral, as described in the request letter to the Federal Reserve, is of lower credit quality or weaker underwriting standards. It appears that the volume of the collateral pledged would not be sufficient and that the Federal Reserve would not be willing to accept the collateral without a substantial haircut.

Supervisory History

The insured legal entities of Citigroup are shown in the table below.

Entities (9/30/2008)	**Assets**	**Deposits**	**CAMELS**	**Exam Date**
Citibank, National Association	1,207,007	748,841	2-2-3-3-3-3/3	4/18/2008
Citibank (South Dakota), N.A.	77,738	42,357	2-2-2-2-2-2/2	11/30/2007
Citicorp Trust Bank, FSB	19,599	7,231	2-2-2-1-1-1/2	2/12/2007
Citibank (Banamex USA)	1,323	1,009	1-2-1-2-1-2/2	1/29/2007
Department Stores National Bank	375	301	2-2-2-2-2-2/2	11/30/2007

Citibank, National Association (CBNA)

The December 31, 2007, OCC Examination of CBNA resulted in a composite rating downgrade to a "3." The OCC issued a Memorandum of Understanding (MOU) against CBNA June 11, 2008 following the 2007 Report of Examination, which was issued in April 2008. The MOU included provisions related to risk management, corporate governance, and the ALLL reserve methodology. It also included additional provisions related to effective Board oversight and the development and implementation of management succession, risk management, liquidity, profit and capital adequacy plans.

Citibank, NA	**1/1/07 OCC**	**1/1/06 OCC**	**1/1/05 OCC**	**1/01/04 OCC**
UFIR	2-2-3-3-3-3/3*	2-2-2-2-1-2/2	1-2-2-2-1-2/2	1-2-2-1-1-2/2
Classifications/T1 +ALLL	20.02%	14.77%	11.19%	Not included
Enforcement Action	None	None	None	None
Financial Data	**9/30/2008**	**12/31/2007**	**12/31/2006**	**12/31/2005**
Total Assets	1,207,007	1,251,715	1,019,497	706,497
Total Loans	628,149	687,790	569,580	388,633
Total Deposits	748,841	782,404	665,743	485,990
Tier 1 Leverage Ratio	6.51	6.65	6.09	6.45
Total Risk Based Capital Ratio	13.38%	13.33%	12.39%	12.55%
Brokered Deposits to Total Deposits	3%	4.55%	5.26%	9.33%

*An interim rating change was affected on 11/30/07.

Citibank (South Dakota), N.A.

Citibank (South Dakota), N.A. is a Competitive Equality Banking Act (CEBA) credit card bank, with no branch banking offices. Citibank (South Dakota) is primarily funded by Citigroup's broker deposit program and credit card securitizations. The cost of funds increased dramatically over the prior year as a result of the rates paid on deposits generated by the broker deposit program. Citibank (South Dakota) is one of the principal sources of interest rate risk for Citigroup bank subsidiaries.

Citicorp Trust Bank, FSB

This thrift originates fixed-rate, nonconforming (nonprime), single-family residential real estate mortgages and private-label credit card loans. The thrift does not have a branch network.

Citibank (Banamex USA)

This non-member bank provides banking services for companies and individuals in Mexico and the United States. Banamex USA offers checking and master accounts, time deposit accounts, electronic funds transfer, foreign exchange, and VISA or MasterCard credit cards for individuals. Banamex USA provides corporate banking products, such as working capital loans, import/export lines of credit, accounts receivable and inventory financing, commercial and stand-by letters of credit, and deposit and investment accounts. Banamex USA was founded in 1963 as Community Bank of San Jose and changed its name to California Commerce Bank, Inc. in 1980, and finally changed its name to Citibank (Banamex USA) in 2006.

Department Stores National Bank (DSNB)

DSNB is the credit card issuer of Visa and retail private label accounts for Citigroups' relationship with Macy's Inc. DSNB is a subsidiary of Citibank (South Dakota), N.A., and does not have any employees or any branch banking offices. All servicing of DSNB's accounts is currently provided by affiliates and third parties.

Systemic Risk

It appears likely that any transaction implemented by the FDIC under a least-cost framework would have significant adverse effects on economic conditions and the financial markets based on Citigroup's size and the markets in which it operates. Given Citigroup's significant international presence, effects on money market liquidity could be expected on a global basis. Term funding markets remain under considerable stress. These pressures have increased over the past week with a loss of investor confidence in financial institutions' performance, as evidenced by a significant drop in bank equity values and another round of increases in banks' credit default swap spreads. Citigroup has been particularly vulnerable with its exposure to credit and market losses coupled with its dependence on international operations for funding.

The risk profile of Citigroup is increasing rapidly due to of deteriorating liquidity and poor asset quality. Liquidity pressures have reached crisis proportions, such that Citigroup and its five insured entities will be unable to meet obligations. Staff projects that Citigroup will be unable to pay obligations or meet expected deposit outflows during the week beginning November 24, 2008 if there is not a systemic risk determination and implementation of proposed measures to improve market perception on Monday morning. The FDIC is prohibited from taking action that could expose the deposit insurance fund in a manner that could to benefit debt or equity holders of a company without invocation of the systemic risk exception available under the FDI Act.

Conclusion

Not providing open bank assistance to Citigroup would likely have major systemic effects. Both financial stability and overall economic conditions would be adversely affected for the reasons discussed above, and staff believes the consequences could extend to the broader economy. Disruptions to global money and credit markets since September have resulted in sharp downturns among major coincident indicators of real economic activity. The index of industrial production published by the Federal reserve Board declined by 4.2 points in September – its largest point decline ever and the largest decline in percentage terms in over 50 years. Retail sales fell 2.8 percent in October, the largest monthly decline in over 20 years, exceeding even the monthly decline immediately following the September 2001 terrorist attacks. Payroll jobs declined by 240,000 in October and a revised 284,000 in September as employers reacted to financial market uncertainty by cutting back on positions. These developments point to a clear nexus between financial market turmoil and impaired economic performance that could be expected to worsen further if Citigroup and its insured subsidiaries should be allowed to fail. Such an event would significantly undermine business and household confidence. In addition, with the liquidity of banking organizations further reduced and their funding costs increased, banking organizations would become even less willing to lend to businesses and households. These effects would contribute to weaker economic performance, further damage financial markets, and have other material negative effects.

In creating the systemic risk exception, Congress clearly envisioned that circumstances could arise in which the exception should be used. In view of the current intense financial strains, as well as the likely consequences to the general economy and financial system of a failure to provide open bank assistance to the third-largest commercial bank in the United States, staff believes that circumstances such as Congress envisioned are clearly present and that invocation of the systemic risk exception is justified.

This recommendation is supported by:

John V. Thomas
Acting General Counsel

RESOLUTION

WHEREAS, staff has presented information to the Board of Directors ("Board") of the Federal Deposit Insurance Corporation ("FDIC") indicating that the recent unprecedented disruption in credit markets and the resultant effects on the abilities of banks to fund themselves and to intermediate credit place the United States in danger of suffering adverse economic conditions and financial instability; and

WHEREAS, these conditions threaten the stability of a significant number of insured depository institutions, thereby increasing the potential for losses to the insurance fund in the resolutions of such insured depository institutions; and

WHEREAS, staff has advised the Board of Directors ("Board") of the Federal Deposit Insurance Corporation ("FDIC") that Citibank (South Dakota), National Association, Las Vegas, Nevada, Citibank, National Association, Sioux Falls, South Dakota, Citicorp Trust Bank, Federal Savings Bank, Wilmington, Delaware, Citibank (Banamex USA), Century City, California, Department Stores National Bank, Sioux Falls, South Dakota ("Banks"), and their affiliates are in seriously weakened condition; and

WHEREAS, staff has advised that severe financial conditions exist which threaten the stability of the Banks which are insured depository institutions possessing significant financial resources; and

WHEREAS, a proposal for the stabilization of the Banks and their affiliates without the appointment of the FDIC as receiver has been developed in consultation with the Board of Governors of the Federal Reserve System ("Federal Reserve Board") and the Secretary of the Treasury ("Treasury") (collectively the "Agencies"), which involves the Agencies provision of guarantees against loss on certain residential assets for 10 years and certain other assets for a period of 5 years; and

WHEREAS Citigroup Inc. ("Citigroup") will take a first loss position equal to $37 billion; and

WHEREAS for losses above $37 billion there is a loss sharing agreement where losses are shared 10 percent by Citigroup and 90 percent by the Agencies with Treasury taking a second loss position up to $5 billion, the Corporation taking a the third loss position up to $10 billion, and the Federal Reserve having agreed to take the remaining risk based on nonrecourse lending on the pool of assets ("Proposal"); and

WHEREAS the Corporation is receiving $3 billion in preferred stock as compensation for its taking the $10 billion third loss position; and

WHEREAS, the Proposal is subject to prudential regulatory oversight, with the guarantees having a limited duration, and staff believes that the Proposal will avoid or mitigate the serious adverse effects on economic conditions or financial stability in the most cost effective method; and

WHEREAS, the Corporation, OCC, and OTS have determined that the bank meets the conditions under Section 13 (c) 8(A)(i) and (ii) of the FDI Act for receiving direct financial assistance before the appointment of a receiver; and

WHEREAS, staff has recommended that the FDIC Board make a systemic risk recommendation supporting action by the FDIC; and

WHEREAS the Corporation has been advised that the Board of Governors of the Federal Reserve System ("Federal Reserve Board") is expected to make a similar recommendation and that the Secretary of the Treasury ("Treasury"), after consultation with the President, is expected to make the systemic risk determination in this situation.

NOW, THEREFORE, BE IT RESOLVED, the Board finds that the instability of the Banks would have serious adverse effects on economic conditions or financial stability and would create systemic risk to the credit markets; and

BE IT FURTHER RESOLVED, that severe financial conditions exist which threaten the stability of a significant number of insured depository institutions or of insured depository institutions possessing significant financial resources and the Banks are insured depository institutions under such threat of instability and that the Board takes this action in order to mitigate the serious adverse effects, which will lessen the risk to the insurance fund, and systemic risks, posed by the Banks, and that the proposal will be the least costly of all available methods;

BE IT FURTHER RESOLVED, that the Board finds that the Proposal which involves the provision of assistance under section 13(c)(2) of the Act, 12 U.S.C. § 1823(C)(2), in the form of guarantees against loss to, or contributions to, the Banks, will mitigate the serious adverse effects on economic conditions or financial instability that would be caused by the Banks' continued seriously weakened condition; and

BE IT FURTHER RESOLVED, the Board finds that the conditions for receiving direct financial assistance before the appointment of a receiver under Section 13 (c) 8(A)(i) and (ii) of the FDI Act have been satisfied, and

BE IT FURTHER RESOLVED, the Board hereby authorizes the Chairman, or her designee, to provide the written recommendation to the Secretary of the Treasury specified under section 13(C)4)(G)(i) of the Act, 12 U.S.C. § 1823(C)(4)(G)(i); and

BE IT FURTHER RESOLVED, the Board hereby authorizes the Director, DRR, or his designee, and all other FDIC staff to take all appropriate action to implement the provision of assistance authorized hereunder, including but not limited to: credit support in the form of loan guarantees, and loss sharing; and to take any other action necessary and appropriate in connection with this matter.

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Executive Secretary