Hughes Hubbard & Reed

A Retooled General Electric: An Industrial Giant That Is No Longer "Too Big To Fail"

Client Advisories

Hughes Hubbard & Reed LLP • A New York Limited Liability Partnership
One Battery Park Plaza • New York, New York 10004-1482 • +1 (212) 837-6000

July 5, 2016 - In May, we reported on the judicial rescission of MetLife's designation as an entity "too big to fail," and noted that the court's decision provided designated companies with a framework to challenge their designation. Another effective option is to fundamentally change the nature of the business, which is what GE Capital Global Holdings, LLC ("GE") has done over the past three years. As a result, on June 28, 2016, the Financial Stability Oversight Council ("FSOC") determined that GE is no longer too big to fail and released GE from the heightened regulatory standards and oversight imposed upon designated entities. This is first time FSOC has released an entity from the "SIFI" designation.

Three years ago, the FSOC identified GE as a systemically important institution whose failure would pose a threat to the country's financial stability and accordingly, would be subject to a heightened level of regulatory scrutiny, additional capital requirements, and other government oversight. In response, however, GE transformed itself. Working with FSOC staff to assure that its changes would result in a rescission as part of FSOC's annual reevaluations of GE's status, GE made deliberate and significant changes to its business to minimize the risk to the U.S. economy. Its efforts included detangling itself from various financial markets, divesting business lines, and significantly restructuring its operations and corporate structure. In March 2016, GE requested that FSOC rescind its designation. Three months later, the FSOC agreed. Now, only two non-financial institutions remain SIFIs, and experience has proven two paths to de-designation: direct legal challenge or substantial, targeted business restructuring.

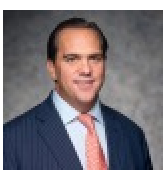
FSOC's rescission of GE's designation provides some insight into what factors matter most for liberating a company from the designation's enhanced standards. One takeaway is that it matters not just to reduce the size of the organization, but how that reduction minimizes potential threat to the country's financial stability. FSOC found that GE had "fundamentally changed its business" and become a "much less significant participant in financial markets and the economy." GE's march to de-designation tracked the core areas of risk that FSOC identified when it first designated GE as too big to fail:

- In 2013, GE had total assets that exceed $549 billion; now, it has divested more than 50 percent of those assets, while at the same time nearly tripling the percent of its liquid assets.
- GE was once the most substantial player in the commercial paper market; now, its presence is nominal.
- At one point, distress at GE could have caused money market funds to buck the dollar; now, no money market funds hold GE commercial paper, eliminating that risk.
- GE once had lines of credit at over fifty banking institutions; now, GE has just a single line of credit to its parent, significantly reducing its direct interconnectedness with large financial institutions (though the parent has lines of credit at over forty banks).
- GE's financing operations had touched over 56 million consumers and businesses; now, its financing transactions relate only to its industrial activity (e.g., aircraft-related lending).
- GE's funding model had a significant (and systemically dangerous) focus on short-term funding; now, GE has increased reliance on long-term debt.
- GE's corporate structure was so complex that distressed restructuring would have been virtually impossible, with the ability to maintain going concern value sacrificed; now, GE has a simplified corporate structure that would lend itself to distressed restructuring, if necessary.

All this is not to say that GE is small, by any means: the FSOC reiterated that GE remains a substantial and complex market participant. The focused yet substantial shift in the nature and scope of GE activities, however, has extricated GE from SIFI status and will allow it to continue to sharpen its focus on its core industrials business.

.

Related People



Anson B. Frelinghuysen

Related Areas of Focus

Corporate Reorganization & Bankruptcy