



MEMORANDUM

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

To: File

From: Bruce Johnson

Date: September 27, 2004

Subject: Meeting with Bushnell, Rollauer, Daley, and Takahisa - Formal Agreement

Purpose of Meeting: Provide update to senior management regarding OCC's analysis of Citi's efforts to comply with the formal agreement.

Date of Meeting: September 16, 2004

OCC Attendees: Bruce Johnson

Bank Attendees: David Bushnell, Thomas Rollauer, Diane Daley, Wendy Takahisa

Conclusions: Productive meeting. I was able to provide to executive management our analysis of the bank's efforts to comply with the formal agreement, including areas where we have concerns. I was also able to ask questions and get additional information.

Introduction: I explained that I wanted to establish a dialogue with this audience to communicate the results of our exam activities with the FA so that we can have an opportunity to correct shortcomings, resolve differences in opinions prior to the Mar-05 exam, and obtain additional information. I also explained that we need to document our work regarding compliance with the formal agreement very carefully and will need to verify actions much more closely than we normally do in supervision.

Details of Discussion:

A. Status of OCC Activities

- (1) GSPM Exam – Systems are still evolving, but are adequate to identify CSFTs and escalate for higher levels of review.
- (2) Fixed Income Derivatives – Found some problems with identification and escalation, but we believe that actions are being taken to tighten systems.
- (3) Equity Derivatives – Not fully completed, but no significant issues identified at this point in time.
- (4) On-going Supervision – Several questions. See below.

B. Areas Needing Improvement

- (1) Reporting to executive management and the Board/Audit Committee needs improvement. The report of > \$500MM OSUC is not sufficient. Bob Martin's UDACS report to the Business Practices Committee is a step in the right direction, but still needs some work. They asked for

suggestions on how to improve the report. I said that I would think about it and ask for others' opinions before getting back to them.

C. Concerns

(1) Relativity and the Boiling Frog Theory – I explained I was concerned that management and committees such as CMAC which are too close to these types of products may become too conditioned and not perceive subtle changes over a longer period of time, much like what happened to real estate lending in the 1980s. I explained that occasionally sending the most extreme deals to David Bushnell and Randy Farmer was a good practice and helped them occasionally dip their fingers in the pot to insure the water was not getting too hot. If they were involved with every deal, they, too, may become conditioned and lose objectivity. The BPCs may also be a control point for this risk since they do not see every deal, but only those furthest on the edge. However, this is still a risk which they will need to watch carefully.

(2) Complexity of Communications in the Citigroup Environment –I'm concerned with the company's ability to effectively distribute communications to such a vast and complex company, particularly when there are so many policies and directives concerning CSFTs which come from so many sources. We noted a couple of errors in communications made by senior level managers in control functions, who are in part responsible for controlling CSFTs, which demonstrates how difficult it is to keep everything straight. I noted that GSPM and the SCF product groups were overcoming this obstacle by the use of templates and checklists to include the requirements of all of the various policies and directives. Examples are the SPAW in AFG and the Deal Ticket in IEF.

(3) Tax – We have received indications that regulators' appetite, or tolerance, for tax products has greatly decreased recently. While we cannot point to any official communications, we have noted that it is much more difficult to get licensing approval for issues which have a tax element in 2004 than it was in 2003. David Bushnell said they have noticed the same thing and have tightened up their tax policies again in response. Policies were tightened in early 2004 and again later in this year to require a higher percentage of non-tax economic benefit in a deal before it would be approved. From a previous meeting Chris Dark and Diane Daley arranged a meeting for me with Keith Anzel of their tax department on September 29.

D. Questions

(1) How are CSFTs defined in non-GCIB business units? The Citigroup Structured Finance Policy covers the entire corporation, but the definition of a "covered transaction" is not broad enough to comply with the formal agreement's requirement to define CSFTs. Other policies fill this gap such as the GCIB CMAC policy, the Tax Policy, the Legal Vehicle Policy and others, but not all of these policies apply to non-GCIB businesses. Diane Daley provided me with copies of excerpts of policies of non-GCIB business units which explain how "one-off" transactions and new products are vetted and approved.

(2) What is meant by, "Quarterly due diligence procedures will help ensure facilitation of annual Business Heads certification to the OCC," as noted in the Global Compliance Update to the

Audit Committee in July 2004? Per Tom Rollauer this is referring to a report on the status/completion/efficacy of the Business Units' RCSAs.

(3) How can I arrange to see the listing of "potentially abusive tax shelters" which is required to be maintained per Citi's Tax Policy? David Bushnell asked Diane Dailey to follow up and see what lists are maintained. One is maintained as a requirement for the IRS and is essentially a public document.

Follow-up

(1) David Bushnell said this meeting was very beneficial to him and asked if we could do this quarterly. We tentatively plan to meet again in December.

(2) Meet with Keith Anzel of Citi's tax department.

(3) Follow-up on issue of definition of CSFTs in non-GCIB business units, including trying to determine if there are any transactions in those units which may actually be CSFTs and are not a "covered transaction" or covered in scope by the Citigroup tax policy.

(4) Insure that Citi maintains a listing of "potentially abusive tax shelters." Review lists over period of time. See if any trends exist.