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Via Electronic Mail

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Re: Proposed Changes to Applicability Thresholds for Regulatory Capital Requirements for Certain U.S. Subsidiaries of Foreign Banking Organizations and Application of Liquidity Requirements to Foreign Banking Organizations, Certain U.S. Depository Institution Holding Companies, and Certain Depository Institution Subsidiaries (Docket ID OCC-2019-0009, RIN 1557-AE63; FRB Docket No. R-1628B, RIN 7100-AF21; FDIC RIN 3064-AE96); Prudential Standards for Large Foreign Banking Organizations; Revisions to Proposed Prudential Standards for Large Domestic Bank Holding Companies and Savings and Loan Holding Companies (FRB Docket No. R-1658, RIN 7100-AF45)

Ladies and Gentlemen:

The Bank Policy Institute[1] and the American Bankers Association[2] appreciate the opportunity to comment on (i) the proposal issued by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency regarding the agencies' proposed changes to the applicability thresholds for certain regulatory capital requirements and the application of liquidity requirements to

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1 The Bank Policy Institute is a nonpartisan public policy, research and advocacy group, representing the nation's leading banks and their customers. Our members include universal banks, regional banks and the major foreign banks doing business in the United States. Collectively, they employ almost 2 million Americans, make nearly half of the nation's small business loans, and are an engine for financial innovation and economic growth.

2 The American Bankers Association is the voice of the nation's $18 trillion banking industry, which is composed of small, regional, and large banks that together employ more than 2 million people, safeguard nearly $14 trillion in deposits, and extend more than $10 trillion in loans. Learn more at www.aba.com.

foreign banking organizations ("FBOs") that have "significant" U.S. operations[3] and (ii) the proposal issued by the Federal Reserve regarding proposed changes to the enhanced prudential standards for large FBOs and revisions to previously proposed changes to the enhanced prudential standards for large bank holding companies and savings and loan holding companies.[4] We are submitting one comment letter on both proposals because they are interrelated and would use a generally similar methodology.

We appreciate the agencies' efforts to implement the Economic Growth, Regulatory Relief, and Consumer Protection Act ("EGRRCPA") and to tailor the application of enhanced prudential standards under Section 165 of the Dodd-Frank Act, as well as the capital and liquidity requirements for the U.S. operations of FBOs. A tailored regulatory framework that appropriately aligns regulatory requirements with the diverse activities, organizational structures, business and regulatory models and risk profiles of FBOs would further the policy objectives of fairness and effectiveness in regulation.[5] Such a framework would also promote global cooperation and the development of a global regulatory framework in which home-country regulation and host-country regulation are balanced appropriately.

We are concerned, however, that the proposals represent a missed opportunity because they would not create an appropriately tailored regulatory framework for FBOs. Most significantly, by using the characteristics of an FBO's combined U.S. operations ("CUSO") to determine the liquidity requirements and many of the enhanced prudential standards applicable at the level of an FBO's U.S. intermediate holding company ("IHC"), the proposals would create a complex and inappropriate regulatory framework in which regulatory requirements at the IHC level would often be misaligned with the IHC's activities, organizational structure, business model and risk profile. The proposed framework, which could increase *ex-ante* ring-fencing, could undermine global regulatory cooperation and the ability of global regulators to achieve an appropriate balance between home- and host-country regulation. Applying standards to an IHC that are significantly more stringent than those applicable to a similarly situated U.S. BHC would also undermine principles of national treatment and competitive equality. Accordingly, we urge the agencies to revise the proposals so that the application of each liquidity requirement and enhanced prudential standard at the IHC level is based solely on the characteristics of an FBO's IHC.

The proposed framework appears predicated on the view that an FBO is a source of risk—rather than a source of strength—for its U.S. operations. Section II.A.5 of this comment letter explains why concerns about FBOs presenting risks to their U.S. operations are misplaced, including in light of the global post-crisis regulatory framework that has reinforced the resiliency of FBOs and improved their ability to support U.S. operations in times of stress. In particular, internal total loss-absorbing capacity ("TLAC") requirements have obligated most FBOs with significant U.S. subsidiary operations to "cash collateralize" support for their IHCs in the event of material financial distress.[6] Internal TLAC acts both directly as an available resource, through its significant additional loss-absorbing capacity, and indirectly as a further incentive for the FBO to act as a source of continued support for its IHC. This resource

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[3] 84 Fed. Reg. 24296 (May 24, 2019) (the "interagency proposal").

[4] 84 Fed. Reg. 21988 (May 15, 2019) (the "Federal Reserve proposal").

[5] *See, e.g.*, 12 U.S.C. § 5365(b)(2) (requiring that the Federal Reserve give due regard to the principle of national treatment and equality of competitive opportunity in applying enhanced prudential standards to FBOs); Federal Reserve proposal, 84 Fed. Reg. at 21989 (noting the objective of improving the regulatory framework's simplicity, transparency and efficiency); Federal Reserve, *Supervision and Regulation Report* (May 2019) (the "**Supervision and Regulation Report**"), at 1–2 (discussing the policy goals of efficiency, transparency and simplicity in regulation), *available at* https://www.federalreserve.gov/publications/files/201905-supervision-and-regulation-report.pdf.

[6] The internal TLAC requirements apply to FBOs that are GSIBs and have IHCs. Other non-GSIB FBOs are also stable sources of strength for their U.S. subsidiaries via funding structures that incentivize further parent support and that enhance U.S. financial stability outcomes under stress.

provides a valuable contribution to U.S. financial stability, and it is costly to maintain. A balanced framework for tailoring applicable regulations should account for the FBO as a source of strength as a general matter and for cash-collateralized elements in particular to accord with principles of national treatment and competitive equality.

We do, however, believe that the risk-based indicator methodology underlying the proposals, if properly deployed, calibrated and indexed, is a promising approach that could serve as a fair, transparent and effective means for tailoring the application of capital and liquidity requirements and enhanced prudential standards to the U.S. operations of FBOs. Subject to the critical revision of deploying the methodology so that the risk-based indicators calculated at the IHC level determine IHC-level requirements and standards, as well as several important refinements addressing other aspects of the proposed indicators, we strongly encourage the agencies to adopt the general framework of the risk-based indicator approach as they proceed to implement EGRRCPA.

A properly designed and calibrated regulatory framework for FBOs would take into account the actual risks posed by the structure and operations of the FBOs and the complementary relationship between home and host-country regulation. The various recommendations presented in this letter would improve the regulatory framework in a manner that would better achieve an appropriate balance between home and host-country regulation. Solutions that are particularly compelling are those that apply appropriately "discounted" resource requirements in the host country to account for, among other things, the application of "full" requirements at the parent level in the home country. These solutions would have the benefit of balancing host-country certainty with group flexibility.[7] For GSIB FBOs with IHCs, direct accounting for internal TLAC, in particular, in setting host country resource requirements for IHCs is a sound, sensible means of achieving this balance.

Leaving aside recommended changes to the proposals and responses to questions presented in the proposals, we wish to emphasize that no regulatory tailoring for banking organizations can be effective or complete unless tailoring is also reflected in supervisory expectations and supervision and examination processes. In the BPI comment letter on the tailoring proposals for domestic banking organizations,[8] we explained that the purpose of EGRRCPA will be defeated if compliance with standards that, by regulation, no longer apply to a banking organization are nonetheless imposed in the examination process through matters requiring attention, horizontal reviews or ratings decisions. The purpose of EGRRCPA will also be defeated if uniform supervisory expectations are applied to banking organizations irrespective of their activities, business and regulatory models, organizational structures and risk profiles. For example, for firms in the Federal Reserve's LISCC portfolio, applying uniform expectations would inappropriately result in certain firms needing to meet expectations that are a poor fit for their activities, business and regulatory models, organizational structures and risk profiles. We therefore urge the agencies to identify how they should tailor their supervisory expectations and supervision and examination processes in a manner consistent with the regulatory tailoring being implemented pursuant to EGRRCPA.

We are also deeply concerned that the Federal Reserve proposal has left open the possibility of application of separate liquidity requirements to FBOs' U.S. branches and agencies. One of the justifications for the Federal Reserve's original IHC requirements was that they struck a balance between the need for some level of host-country regulation and the *ex-ante* ring-fencing regime that liquidity requirements for branches and agencies would create. Imposing standardized liquidity requirements on FBOs' U.S. branches and agencies would upset that balance and would likely lead to increased ring-fencing around the world. Moreover, an *ex-ante* ring-fencing regime created by

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7 *See* Vice Chair for Supervision Randal K. Quarles, *Trust Everyone—But Brand Your Cattle: Finding the Right Balance in Cross-Border Resolution*, Harvard Law School, Cambridge, MA (May 16, 2018) (the "**Brand Your Cattle Speech**"), *available at* https://www.federalreserve.gov/newsevents/speech/quarles20180516a.htm.

8 Bank Policy Institute, *Comment Letter re: Regulatory Tailoring and DFAST Proposals* (Jan. 22, 2019) (the "**BPI Domestic Tailoring Comment Letter**"), *available at* https://bpi.com/wp-content/uploads/2019/01/BPI-Comment-Letter-on-Regulatory-Tailoring-and-DFAST-Proposals-Final.pdf.

standardized branch liquidity requirements would be detrimental to the global economy and threatens to expand and deepen the risk of a financial crisis in times of financial stress. Such a ring-fencing regime would inherently create barriers to the free flow of liquidity, capital and other resources to where it is most needed, whether to meet economic demand or to relieve financial stress.

In light of the home and host-country liquidity requirements applicable to FBOs and their U.S. branches and agencies, we do not believe there is a risk that needs to be addressed through an entirely new layer of liquidity requirements for FBO branches and agencies in the regulatory regime. The combination of standardized home-country liquidity requirements (such as the LCR) and existing host-country liquidity regulation and supervision sufficiently addresses liquidity risk at FBOs' U.S. branches and agencies and appropriately balances home- and host-country regulation. We urge the Federal Reserve to consider the implications of adopting such requirements for the prospects of achieving global regulatory cooperation and appropriate balances between home- and host-country regulation.

Finally, to the extent the framework contemplated by the proposals—one in which liquidity requirements, single-counterparty credit limits and other enhanced prudential standards would apply to an FBO's IHC on the basis of the FBO's CUSO characteristics—is in effect a means to regulate indirectly the U.S. branches and agencies of FBOs, there are more effective, less unduly burdensome ways of doing so. Any framework to regulate liquidity at FBOs' U.S. branches and agencies—including, if ultimately proposed, standardized branch liquidity requirements—should, prior to implementation, be discussed at the international level, including among U.S. and non-U.S. financial regulators and both foreign and U.S. banking organizations that are globally active. Further, in order to enable the global competitiveness of the U.S. financial system and promote the policy objectives of national treatment and equality of competitive opportunity and the competitive opportunity of all banking organizations—including U.S. banking organizations that operate globally—any such requirements should be introduced as standards agreed to at the international level.

I. Executive Summary.

- ➢ The final rules should use the characteristics of an FBO's IHC—and not its CUSO—to determine each requirement that applies at the IHC level.
  - Using the characteristics of an FBO's CUSO to determine regulatory requirements at the IHC level would undermine the policy goals of fairness and effectiveness in regulation and could discourage FBOs from participating in the U.S. markets. The agencies could better achieve their supervisory objectives if the regulatory requirements applied at the IHC level were determined on the basis of an IHC's characteristics.
    - o The framework set forth in the proposals is unnecessarily complex and at odds with the Federal Reserve's stated objective of improving upon the existing regulatory framework's simplicity.
    - o The proposals would not achieve appropriate tailoring for FBOs because the application of most IHC-level requirements would be based on the characteristics of the parent FBO's CUSO.
    - o The proposed framework would be inefficient because of the inherent disconnect between regulatory requirements and risk resulting from the application of more stringent IHC-level requirements on account of the characteristics of the parent FBO's CUSO.

    - Increasing the stringency of applicable liquidity and other requirements could discourage FBOs from participating in the U.S. market, which could have a detrimental effect on borrowers and the economy generally and could lead to reduced financial system resiliency as a result of increased market fragmentation.

    - The supervisory objectives of the proposals could be achieved by setting liquidity requirements and other standards (including single-counterparty credit limits) on the basis of the IHC's own characteristics.

  - If the agencies nevertheless implement a framework that would apply regulatory requirements to an FBO's IHC on the basis of characteristics of the FBO's CUSO, they should further tailor the application of the requirements to better reflect the IHC's actual risk profile.

  - Revising the proposals to account for the application of home-country standards to FBOs on a consolidated basis and the implications for IHC and CUSO liquidity could promote global cooperation and a global regulatory framework in which home-country and host-country requirements are more appropriately balanced.

- The agencies should adopt the general framework of the risk-based indicator approach set forth in the proposals, subject to deploying it so that an IHC's characteristics determine IHC-level requirements, as discussed above, and to other important changes that would more appropriately tailor prudential requirements to the risk profiles of applicable FBOs.

  - The wSTWF risk-based indicator should be changed in the final rules to exclude funding from affiliates and to more appropriately reflect underlying asset liquidity.

    - Consistent with the cross-jurisdictional activity risk-based indicator, the final rules should exclude from the calculation of wSTWF funding from non-U.S. affiliates.

    - The agencies should revise the components of wSTWF to better reflect actual liquidity risk.

    - The agencies should revise the components of wSTWF to take into account underlying asset liquidity.

    - Risks relating to the use of short-term funding are already mitigated significantly by liquidity requirements applicable to FBOs on a global, consolidated basis under home-country regulations and by sources of funding available to IHCs.

  - The nonbank assets risk-based indicator should be reformulated to exclude assets that represent claims on affiliates and to better account for actual risks presented by various types of assets currently deemed to be "nonbank assets" under the proposals.

    - Consistent with the cross-jurisdictional activity risk-based indicator, the final rules should exclude from the calculation of nonbank assets those assets which represent claims on affiliates.

    - The agencies should revise the definition of "nonbank assets" in the final rules to better account for the actual underlying risks of the activities conducted in nonbank subsidiaries.

        - Risks relating to nonbank activities are already mitigated significantly by liquidity and other requirements, including resolution planning requirements, applicable to FBOs on a global, consolidated basis under home-country regulations.

    - The cross-jurisdictional activity risk-based indicator should be revised in the final rules to exclude all transactions with non-U.S. affiliates and to exclude certain other transactions and exposures that are not indicative of a heightened risk profile.

    - The off-balance-sheet exposures risk-based indicator should be adjusted in the final rules to better account for FBO organizational structures and to incorporate risk-sensitive measures.

    - The agencies should not subject banking organizations to Category II standards on the basis of meeting a higher threshold for one or more of wSTWF, nonbank assets and off-balance-sheet exposures.

    - The final rules should provide for annual adjustments to the dollar thresholds used to assign firms to different categories to account for economic growth by indexing these dollar thresholds to the growth in domestic banking assets.

    - Recommendations with respect to the risk-based indicator framework set forth in the BPI domestic tailoring comment letter also apply to the framework set forth in the proposals.

- ➢ The final rules should incorporate transition periods for those FBOs that would be subject to more stringent requirements, including single-counterparty credit limits and certain reporting obligations, as a result of the revised framework.

- ➢ The recommendations with respect to the capital and liquidity frameworks set forth in the BPI domestic tailoring comment letter also apply to the frameworks set forth in the proposals.

    - The agencies should revise the liquidity framework in the final rules applicable to FBOs consistent with our recommendations to the domestic tailoring proposals.

    - The agencies should revise the capital framework in the final rules applicable to FBOs consistent with our recommendations to the domestic tailoring proposals.

- ➢ The Federal Reserve should revise the stress testing requirements under the capital plan rule to provide meaningful relief for Category III firms during the "off" year of the DFAST stress testing cycle.

- ➢ The agencies should not create a $50 billion wSTWF threshold that would subject both domestic and foreign Category IV firms to more stringent liquidity requirements.

- ➢ FBOs should not be required to report for the CUSO data unrelated to the risk-based indicator framework set forth in the proposals.

- ➢ The Federal Reserve should revise the definition of "highly liquid assets" in Regulation YY to expressly include HQLA under the LCR.

- ➢ The agencies should not impose standardized liquidity requirements on FBOs with respect to their U.S. branch and agency networks.

- The agencies should address in the final rules certain technical matters related to the reporting forms underlying the regulatory framework.

II. The final rules should use the characteristics of an FBO's IHC—and not its CUSO—to determine each requirement that applies at the IHC level.

The proposals would assign all FBOs with $100 billion or more in U.S. assets to one of three categories based on their size and other "risk-based indicators." Similar to the domestic tailoring proposals,[9] for purposes of assigning FBOs to one of the three categories, the proposals set a threshold of $75 billion for each of four risk-based indicators (other than size): cross-jurisdictional activity, weighted short-term wholesale funding ("wSTWF"), nonbank assets and off-balance-sheet exposures. Also consistent with the domestic tailoring proposals, FBOs would be assigned to Category II if they have $700 billion or more in U.S. assets or $75 billion or more in cross-jurisdictional activities, to Category III if they have $250 billion or more, but less than $700 billion, in U.S. assets or $75 billion or more in one of the other three risk-based indicators and to Category IV if they have $100 billion or more, but less than $250 billion, in U.S. assets and do not exceed the $75 billion threshold for any risk-based indicator.[10] FBOs with $100 billion or more in total global consolidated assets but less than $100 billion in U.S. assets would not be assigned to a designated "category" but would generally be subject to requirements that are less stringent than those applicable to institutions in Category IV.

Unlike the domestic tailoring proposals, however, the proposals would create an exceedingly complex and conceptually flawed regulatory framework that would, for most requirements, impose requirements for one part of an institution—namely, the IHC—based not on its own characteristics but on the characteristics of the parent FBO's CUSO. For standardized liquidity requirements, liquidity-related enhanced prudential standards, and certain other enhanced prudential standards (including risk management requirements and single-counterparty credit limits) applicable to an IHC, it is not the characteristics of the IHC that would determine its applicable tailoring category but instead the characteristics of an FBO's CUSO. It is only for regulatory capital requirements and capital-related enhanced prudential standards that the characteristics of the IHC would determine the applicable tailoring category. This complexity is compounded because standardized liquidity requirements would apply to the FBO with respect to its IHC and, for certain tailoring categories, to any subsidiary depository institution with $10 billion or more in total consolidated assets (a "covered depository institution subsidiary"); liquidity-related and certain other enhanced prudential standards would apply, depending on the requirement, to one or more of the FBO, its IHC, its U.S. branches and agencies and its CUSO; and regulatory capital requirements would apply to both the IHC and any subsidiary depository institution, but capital-related enhanced prudential standards would apply only to the IHC. The proposals provide little or no rationale for these differentiations or the overall complexity.

The result is regulatory requirements that, as applied at the IHC level but based on non-IHC metrics, may be a poor fit for the IHC's risk profile, creating significant regulatory and operational burdens that are incredibly impactful without a corresponding supervisory benefit. The impact is illustrated in the charts below which show, as an example, IHCs' liquidity standard categories under circumstances in which such categories are based on the IHCs' own characteristics versus the CUSOs' characteristics.

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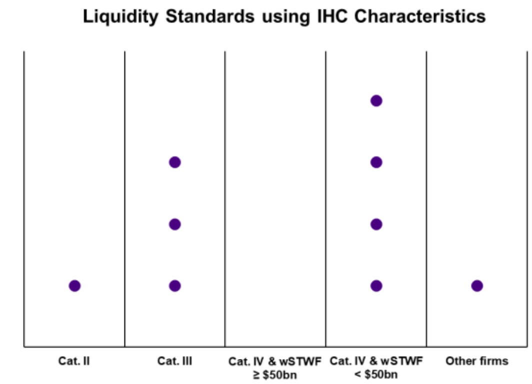
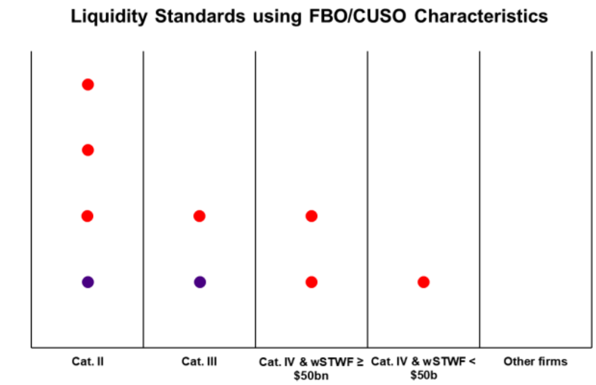
9 83 Fed. Reg. 61408 (Nov. 29, 2018) (the "**Federal Reserve domestic tailoring proposal**"); 83 Fed. Reg. 66024 (Dec. 21, 2018) (the "**Interagency domestic tailoring proposal**").

10 The proposals would not include a fourth category (Category I) included in the domestic tailoring proposals that would apply only to U.S. G-SIBs. There is no such category for FBOs because, under the Federal Reserve's capital rules, only a top-tier U.S. BHC can be identified as a U.S. GSIB. *See* Federal Reserve proposal, 84 Fed. Reg. at 21992 n.28; *see also* 12 C.F.R. Part 217 Subpart H.



Note: Sample includes 9 IHCs that provided FR Y-15 data of the combined IHC and U.S. branch and agency operations of the FBO.



Note: Sample includes 9 IHCs that provided FR Y-15 data of the combined IHC and U.S. branch and agency operations of the FBO.

A. Using the characteristics of an FBO's CUSO to determine regulatory requirements at the IHC level would undermine the policy goals of fairness and effectiveness in regulation and could discourage FBOs from participating in the U.S. markets. The agencies could better achieve their supervisory objectives if the regulatory requirements applied at the IHC level were determined on the basis of an IHC's characteristics.

1. The framework set forth in the proposals is unnecessarily complex and at odds with the Federal Reserve's stated objective of improving upon the existing regulatory framework's simplicity.

The proposals effectively create eight categories, and an FBO with an IHC would be assigned to two categories, which may or may not be the same—a CUSO category and an IHC category: CUSO Category II; CUSO Category III; CUSO Category IV; CUSO non-categorized (if the total consolidated assets of the combined U.S. operations are $50 billion to $100 billion); IHC Category II; IHC Category III; IHC Category IV; IHC non-categorized (if the IHC's total consolidated assets are $50 billion to $100 billion). As described above, capital-related requirements would be based on the IHC's characteristics and would apply to the IHC, while liquidity-related requirements and certain other enhanced prudential standards (including risk management requirements and single-counterparty credit limits) would be based on the characteristics of the CUSO and would apply to one or more of the FBO, its IHC, its U.S. branches and agencies and its CUSO. In addition, for an FBO's depository institution subsidiaries, the IHC's category would determine the applicable capital requirements and the CUSO category would determine the applicable standardized liquidity requirements.

This complexity would frustrate the Federal Reserve's stated objective of improving upon the existing regulatory framework's simplicity. An overly complex framework can result in "unexpected negative synergies among regulations," and the resulting confusion "does not advance the goal of a safe system."[11] Further, excessive complexity can undermine supervisory efforts to communicate transparently to regulated firms and the public about regulatory requirements.[12]

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11 *See* Vice Chair for Supervision Randal K. Quarles, *Early Observations on Improving the Effectiveness of Post-Crisis Regulation*, American Bar Association Banking Law Committee Annual Meeting, Washington, D.C. (Jan. 19, 2018).

12 *See, e.g.*, Federal Reserve proposal, 84 Fed. Reg. at 21989; Supervision and Regulation Report, at 2 ("**Simplicity** involves developing the Federal Reserve's regulations and supervisory framework without unnecessary complexity, and presenting them in a clear and concise manner. The objective of simplicity complements and supports the efforts of the Federal Reserve to be transparent to supervised institutions and the public on its regulations and supervisory programs.") (emphasis supplied).

2. The proposals would not achieve appropriate tailoring for FBOs because the application of most IHC-level requirements would be based on the characteristics of the parent FBO's CUSO.

Applying regulatory requirements to one part of an institution (the IHC) on the basis of the characteristics of a different part of the institution (the FBO's CUSO, including the U.S. branches and agencies) does not accord with the tailoring goal of the proposals or with principles of national treatment and competitive equality. The application of standards to an institution that appropriately reflect *that* institution's risk profile is what the proposals should be designed to achieve.

The activities, business model and risk profile of an FBO's IHC may be, and often are, very different from those of an FBO's U.S. branches and agencies. For example, an IHC's primary source of funding may be the deposits (including insured retail deposits) at a depository institution subsidiary, while the FBO's U.S. branches and agencies may use wholesale funding as a primary funding source. Nonetheless, under the proposals, the IHC-level and depository institution subsidiary-level liquidity requirements would be based on characteristics of the CUSO even though the characteristics of the FBO's U.S. branches and agencies may have little or no relationship to the activities, business model and risk profile of the IHC and its depository institution subsidiary. For example, if the CUSO had wSTWF of $75 billion or more on account of the funding profile of the U.S. branches and agencies and the IHC itself had no wSTWF, the IHC and its depository institution subsidiary would nonetheless be subject to more stringent liquidity requirements for reasons that are unrelated to their activities, business model and risk profile. In other words, an IHC would be subject to the same special liquidity requirements if it had zero wSTWF, provided that the FBO's CUSO had $75 billion in wSTWF, as it would if the IHC itself had $75 billion in wSTWF.

The same principle applies to each requirement that would be applied at the IHC level on the basis of the characteristics of the FBO's CUSO. In particular, whether single-counterparty credit limits are appropriate for an IHC—and, if they are, how those limits could be applied appropriately to an IHC—should depend on the characteristics of the IHC, not the CUSO. Nonetheless, under the proposals, if an FBO's CUSO has $250 billion or more in assets or $75 billion or more in any risk-based indicator, the FBO's IHC, even if it has only $50 billion in assets and minimal amounts of risk-based indicators, would be required to comply with single-counterparty credit limits as they currently would apply to an IHC with $250 billion or more in assets irrespective of the actual characteristics of the IHC and whether such stringent requirements are appropriate for the IHC in light of its activities, business model and risk profile.

If finalized as proposed, the framework could have a disproportionate impact on FBOs based on their organizational structures and could be especially burdensome for depository institution subsidiaries that are consolidated under an FBO's IHC. An IHC's U.S. depository institution subsidiary should not be subject to a requirement that would not apply to that entity but for the characteristics of the FBO's CUSO.[13]

Rather than tailoring IHC-level requirements to the characteristics of the IHC, the proposals would arbitrarily apply requirements that may be a poor fit by also using the characteristics of the FBO's U.S. branches and agencies to determine the applicable requirements. The proposals would thus frustrate the policy objective of fairness and effectiveness in regulation by failing to tailor regulatory requirements based on the characteristics of the IHC and by imposing undue regulatory burdens that are not necessary to achieve the agencies' supervisory objectives.[14]

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13 A depository institution should only be subject to the LCR and proposed NSFR if the IHC parent is a Category II or III institution (based on its own characteristics) and the depository institution has over $10 billion in assets. This will result in consistent treatment of all U.S. depository institutions regardless of whether they are subsidiaries of FBOs or U.S. BHCs.

14 *See, e.g.*, Federal Reserve proposal, 84 Fed. Reg. at 21989; Supervision and Regulation Report, at 1 ("**Efficiency** involves two components. The first is related to methods: efficient methods tailor the requirements and intensity of regulations and supervision

Further, by applying requirements to the IHC on the basis of the CUSO's characteristics, the agencies create a system whereby similarly situated institutions—IHCs and top-tier BHCs with a similar size and risk profile—are subject to very different regulatory requirements. This significantly undermines the principles of national treatment and competitive equality with respect to FBOs operating in the United States.

3. The proposed framework would be inefficient because of the inherent disconnect between regulatory requirements and risk resulting from the application of more stringent IHC-level requirements on account of the characteristics of the parent FBO's CUSO.

The framework set forth in the proposals appears predicated on the assumption that risks affecting an FBO's U.S. branches and agencies would also directly affect the IHC such that they would effectively be the IHC's own risks. For example, the Federal Reserve proposal asserts that "funding vulnerabilities at a U.S. branch can expose [an FBO's] other U.S. operations to heightened liquidity risk because their customers and counterparties may not distinguish liquidity stress at one component of the U.S. operations from the liquidity position of another part of the U.S. operations."[15] We do not believe that this is a fair assumption. As described above, the risk profile of an FBO's IHC may be fundamentally different from the risk profile of the FBO's U.S. branches and agencies, and the proposals do not include any data to support the assertion that risks affecting one part of an FBO's U.S. operations would be likely to affect another part of its U.S. operations. The proposed framework also appears to reflect an assumption that applying more stringent requirements at the IHC level could mitigate risks relating to the FBO's U.S. branches and agencies and that sophisticated funders do not understand the difference between an FBO's U.S. subsidiary operations and its U.S. branch and agency operations.[16] We do not believe this assumption, which substantially increases applicable regulatory requirements, is warranted in the absence of an articulated and persuasive empirical record. Rather, the proposals would inefficiently *increase* the existing regulatory burden for IHCs without addressing any actual, demonstrated risk.

The proposals would have the effect of increasing the regulatory burden for certain FBOs, such as those with IHCs not directly subject to the LCR or those IHCs currently subject to the modified LCR but which would become subject to the reduced or full LCR with more stringent requirements and greater compliance burdens, including as a result of daily calculation requirements. The proposals would also significantly increase the regulatory burden for IHCs with less than $250 billion in assets that become subject to more stringent and burdensome single-counterparty credit limits as a result of the FBO's CUSO crossing the Category II or III thresholds. These changes would present significant operational costs and challenges for those FBOs without providing a corresponding benefit to the U.S. financial system. Consider, for example, an FBO with an IHC with less than $250 billion in assets and less than $50 billion for each risk-based indicator but branch operations that meet the threshold for Category II or III. The framework contemplated by the proposals would subject the IHC to Category II or III liquidity standards and single-counterparty credit limits, even though, on its own, it would not cross the threshold for any such standards or requirements. Notwithstanding the fact that the IHC in this example is small relative to the remainder of the CUSO and has a different risk profile compared to the U.S. branches and agencies, the IHC would be required to maintain a costly enhanced liquidity position, and the need for the IHC to comply with daily calculation requirements applicable

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programs based on the asset size and complexity of firms. Efficient methods also minimize compliance burdens generally while achieving supervisory objectives.") (emphasis supplied).

15 Federal Reserve proposal, 84 Fed. Reg. at 21990.

16 As we note below, the increased IHC-level liquidity requirements would in many cases be met by increasing the funding levels of the IHCs' subsidiary depository institutions, which raise substantial funding through retail deposit-taking. The view that increased liquidity at the IHC would effectively offset corresponding liquidity risk at the branches and agencies is at odds with fundamental assumptions underlying the agencies' LCR rules, which assign different outflow rates to retail and non-retail deposits, as well as applicable legal restrictions.

to institutions subject to the reduced or full LCR would impose an undue compliance burden. The same concern applies with respect to single-counterparty credit limits because any IHC subject to Category II or III standards would be subject to single-counterparty credit limits as they currently apply to IHCs with $250 billion in assets or more, including basing the limits on tier 1 capital and requiring the IHC to apply a specialized treatment for exposures to special purpose vehicles and the economic interdependence and control relationship tests to aggregate certain connected counterparties. The application of more stringent IHC-level requirements would also not relate to any risks relating to the activities, business model and risk profile of the FBO's U.S. branches and agencies, which are what lead to more stringent IHC-level requirements.

Importantly, the mandated increase in liquidity at the IHC level would not address two concerns that have been expressed about the consequences of liquidity risk at the FBO's U.S. branches and agencies: (1) a situation where the FBO's U.S. branches and agencies are experiencing a liquidity shortage and need funding, and (2) a situation where a liquidity crisis at the U.S. branches and agencies results in a corresponding liquidity shortage for the IHC. With respect to the first, existing legal and regulatory requirements would limit the enhanced liquidity position at the IHC from being used to address the liquidity needs of the FBO's U.S. branches and agencies. In many cases, the increased IHC-level liquidity requirements would be met by increasing the funding levels of the IHCs' subsidiary depository institutions, which raise substantial funding through retail deposit-taking and other deposit-taking activities. However, Section 23A of the Federal Reserve Act and the Federal Reserve's Regulation W restrict the ability of depository institutions held under the IHC to act as a source of liquidity to an affiliated branch or agency. With respect to the second, the perceived problem is unlikely to arise given the funding characteristics of many IHCs. It is not necessary to apply more stringent liquidity requirements with respect to an FBO's IHC in order to "protect" the IHC from liquidity risk at the FBO's branches and agencies. In particular, IHCs can have—and many do have—subsidiary depository institutions that raise substantial funding through retail deposit-taking activities, which offer a stable and low-cost source of funding.

The concern that an FBO's branches and agencies would be a source of risk for its IHC is misplaced. The proposed application of more stringent liquidity requirements at the IHC level to address liquidity risk at the FBO's U.S. branches and agencies does not take into account the role of home-country liquidity requirements and Regulation YY liquidity requirements in mitigating liquidity risk for FBOs' U.S. branch and agency operations. Moreover, Section 165 of the Dodd-Frank Act directs the Federal Reserve, in applying enhanced prudential standards to FBOs, to take into account the extent to which an FBO is subject, on a consolidated basis, to home-country standards that are comparable to those applied to financial companies in the United States.[17]

Further, the proposed framework of applying more stringent IHC-level requirements on the basis of the characteristics of the FBO's U.S. branches and agencies would have the result of increasing misallocation risk and resulting inefficiencies.[18] Applying full requirements in the host jurisdiction increases misallocation risk and effectively increases consolidated requirements for the FBO because of the requisite high degree of pre-positioning in host jurisdictions and the lack of flexibility to deploy resources throughout the organization. In addition to increasing misallocation risk, excessive pre-positioning creates the risk that other host authorities will, as a result of a collective

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[17] 12 U.S.C. § 5365(b)(2).

[18] "Misallocation risk" refers to the risk that, due to required pre-positioning of resources in certain legal entities and/or jurisdictions, there will not be sufficient available resources to deploy to match the distribution of losses within the group in an actual financial distress scenario. The agencies note that the proposed LCR requirement for IHCs is not expected to require an FBO to acquire additional high-quality liquid assets ("HQLA") above what it currently holds to meet its global LCR requirements. Rather, in the agencies' view, the interagency proposal's requirements would generally address the location of where HQLA are held in light of the fact that the LCR requirements applicable to IHCs are based on the Basel LCR standard. *See* Interagency proposal, 84 Fed. Reg. at 24314. Even if the replication of home-country requirements in a host country did not increase overall requirements (which, as discussed below, is not the case), applying the same requirements at both the top-tier consolidated and sub-consolidated levels would increase misallocation risk.

action problem, push regulatory requirements well above appropriate levels. If many, much less all, host authorities were to act independently to require full pre-positioning in their own jurisdictions, this would exacerbate the problem of depleting available resources at the top of the group and would thereby limit the group's ability to allocate resources efficiently and, during stress, to deploy resources where actually needed.

Instead, the proposals should strike an appropriate balance between the value of pre-positioning resources and the value of maximizing the flexibility for an FBO so that it can allocate resources efficiently based on business opportunities and, during periods of stress, to recapitalize or otherwise support subsidiaries and operations when, as and where needed.

4. Increasing the stringency of applicable liquidity and other requirements could discourage FBOs from participating in the U.S. market, which could have a detrimental effect on borrowers and the economy generally and could lead to reduced financial system resiliency as a result of increased market fragmentation.

Applying more stringent liquidity standards and other requirements (in particular single-counterparty credit limits) to an FBO's IHC on the basis of the characteristics of the CUSO could further discourage FBOs from participating in the U.S. market, where they play a significant role. "[FBOs] operate in the United States across a spectrum of business models and sizes, ranging from a single U.S. branch to mid-sized banks with traditional retail footprints to some of the largest broker-dealers in the United States. FBOs represent 20% of total U.S. banking system assets, provide about one-third of U.S. business loans, and comprise more than half of the 23 primary dealers for the Federal Reserve Bank of New York."[19] There has been a documented decrease in FBO participation in the U.S. market since the implementation of the post-financial crisis regulatory framework,[20] and increasing applicable requirements will only serve to reinforce or hasten FBOs' exiting, or reducing their presence in, the United States.

There is room for recalibration of U.S. IHC prudential standards that would permit FBOs to participate more fully in the U.S. capital markets and credit markets to the benefit of the U.S. economy.[21] The ability and willingness of an FBO to provide support to its IHC (which we discuss below) warrants recalibration of the existing IHC prudential standards and makes the application of more stringent IHC-level requirements on the basis of the characteristics of an FBO's CUSO inappropriate. Appropriately calibrated prudential standards for IHCs would encourage FBOs to allocate resources to their IHCs and promote the ability of IHCs and their subsidiaries to provide credit to the U.S.

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19 U.S. Department of the Treasury, *A Financial System That Creates Economic Opportunities—Banks and Credit Unions*, at 68 (June 2017) (the "**Treasury Report on Banks and Credit Unions**"), *available at https://www.treasury.gov/press-center/press-releases/Documents/A%20Financial%20System.pdf*.

20 *See id.*, at 70 ("One of the principal concerns raised regarding the post-crisis regulatory framework for FBOs has been how it has discouraged FBOs' appetite to participate in U.S. markets."); SIFMA, *The Importance of FBOs to U.S. Capital Markets*, at 3 (April 8, 2019), *available at* https://www.sifma.org/wp-content/uploads/2019/04/SIFMA-Insights-The-Importance-of-FBOs-to-US-Capital-Markets.pdf ("Applying global regulatory standards to U.S. footprints has caused FBOs to exit businesses, which could have long-term adverse effects on markets and the economy.").

21 *See* Treasury Report on Banks and Credit Unions, at 71 ("In considering [recalibration of IHC requirements], greater emphasis should be given to the degree to which home country regulations are comparable to the regulations applied to similar U.S. BHCs. Where regulations are sufficiently comparable, FBOs should be allowed to meet certain U.S. requirements through compliance with home country regimes.").

economy and liquidity to U.S. capital markets. At a minimum, the existing IHC prudential standards should not effectively be made more stringent as a result of the tailoring effectuated by the proposals.[22]

In addition to increasing the disparity between domestic and foreign firms' participation in U.S. markets, imposing more stringent requirements on IHCs that are not commensurate with the IHCs' own risk profiles, largely as a result of a flawed calculation methodology, could ultimately lead to increased market fragmentation along geographical lines.[23] The fragmentation of institutions and markets across jurisdictional lines can reduce opportunities for cross-border diversification and risk management, impair market liquidity or even prevent capital and liquidity from being channeled where it is needed in times of stress, each of which could ultimately reduce the resilience of both global and domestic financial systems.[24]

5. The supervisory objectives of the proposals could be achieved by setting liquidity requirements and other standards (including single-counterparty credit limits) on the basis of the IHC's own characteristics.

The proposals appear predicated on the view that an FBO is a source of risk—rather than a source of strength—for its U.S. operations. For example, the commentary in the preamble of the interagency proposal regarding LCR and NSFR requirements for IHCs, and potential standardized liquidity requirements for branches and agencies, makes clear that these requirements are intended to require FBOs to pre-position liquidity in the United States without regard to the liquidity resources an FBO is able to provide in order to support its U.S. operations.[25]

The view of FBOs as a source of risk to their U.S. operations is inconsistent with the FBOs' own interests and with historical experience. In the case of U.S. branches and agencies of foreign banks, the foreign parent has every incentive to maintain funding to its U.S. branches and agencies, as those are offices of the foreign bank and a U.S. branch or agency is part of the foreign bank. Taking action to create (or omitting to take action to avoid) liquidity stress at part of the bank would not be in the foreign bank's interest. Moreover, following the financial crisis, many FBOs have increased their investments, in terms of both financial support and personnel resources, in their U.S. operations. In many cases, these increased investments have resulted from the implementation of more stringent capital requirements for IHCs and other banking subsidiaries of FBOs. In addition, for certain IHCs, internal TLAC requirements have essentially required the parent FBOs to cash collateralize their capacity to support the IHC in the case of material financial distress affecting the IHC, further incentivizing FBOs to be a source of continued support and enhancing their position as a source of strength to their U.S. operations. In addition, during the financial crisis,

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22 For similar reasons, the agencies should not apply more stringent liquidity requirements to the U.S. branches and agencies of FBOs, as this would also have the effect of limiting FBO participation in the U.S. credit markets—to the detriment of the U.S. economy. See Section X below.

23 *See* Financial Stability Board Report on Market Fragmentation, at 4–5 (June 4, 2019) (the "**FSB Report on Market Fragmentation**"), *available at* https://www.fsb.org/wp-content/uploads/P040619-2.pdf (noting that financial regulation and supervision can give rise to market fragmentation when national or regional rules diverge from each other and particularly when rules require institutions to take duplicative or incompatible actions to comply with overlapping requirements from different jurisdictions).

24 *See id.*, at 1.

25 *See* Interagency proposal, proposal, 84 Fed. Reg. at 24314 ("the proposal would require that [HQLA] be held in the U.S. intermediate holding company to the extent that they are needed to meet the proposed requirement").

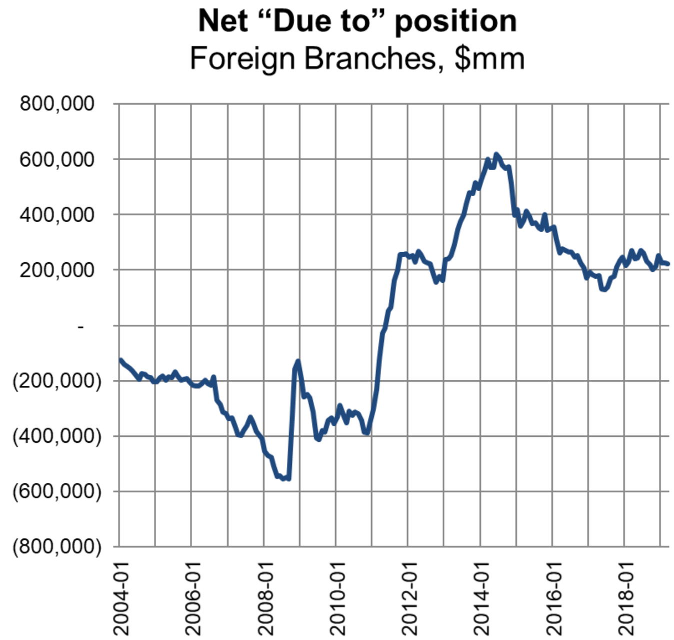
there were many cases of FBOs providing significant support to their U.S. subsidiaries, and even cases of FBOs supporting U.S. entities in which they did not have a controlling interest.[26]

Moreover, following the implementation of the post-crisis regulatory framework, an FBO is a more *resilient* source of strength to its IHC. The description of the risks posed by large FBOs to the U.S. financial system in the preamble to the Federal Reserve proposal largely reflects experiences during the financial crisis and does not take into account the significant regulatory changes since the financial crisis that have substantially mitigated those risks. Those regulatory changes include: more stringent capital requirements; standardized liquidity requirements; liquidity risk management requirements; capital and liquidity stress testing requirements; large counterparty exposure limits; clearing requirements and margin requirements for uncleared swaps; recovery planning requirements; resolution planning requirements and the development of credible resolution plans; and external TLAC requirements. These requirements apply on a global scale to systemically important financial institutions. Notably, all FBOs that would be subject to Category II, III or IV standards under the proposals either are GSIBs or are DSIBs in their home countries and are therefore subject to stringent capital, liquidity and other prudential requirements on a home-country basis. Further, for GSIBs, more stringent host-country requirements currently apply, such as internal TLAC requirements for covered IHCs.

The view of FBOs as a source of financial risk or a "drain" on the U.S. economy may be the result of prior business practice that ended a number of years ago.[27] The concern over this practice should not be the basis of increasing the stringency of prudential requirements because the practice is no longer prevalent. In the years from 2004 through 2010, the U.S. branches of foreign banks frequently borrowed in the U.S. market and lent to their foreign parents, resulting in an overall net "due from" foreign-owned branches position. However, since 2011, the borrowing/lending profiles of U.S. branches of foreign banks have changed, with U.S. branches providing a significant source of funding to the U.S. credit markets. Indeed, since 2011, there is an overall net "due to" foreign-owned branches operating in the United States. The following chart demonstrates the changing position of foreign-owned branches with respect to U.S. markets:

[26] *See, e.g.*, Mitsubishi UFJ Financial Group, Inc., Fed. Res. Bull. (2d Quarter 2011) ("[C]onsummation of the proposal would strengthen Morgan Stanley's capital position and allow Morgan Stanley to better serve its customers"); Press Release, U.S. Department of the Treasury, *$1.7 Billion Additional TARP Funds Returned to Taxpayers, Positive Return on TARP Bank Programs Reaches $10 Billion* (July 5, 2011 (announcing that Bank of Montreal had purchased the remaining TARP-related securities of Marshall and Ilsley Corporation in connection with its acquisition of the company); Press Release, *Banco Santander to acquire Sovereign Bancorp* (Oct. 13, 2008), https://www.santander.com/csgs/Satellite/CFWCSancomQP01/en_GB/Santander/Press-Room/Press-Releases/Banco-Santander-to-acquire-Sovereign-Bancorp.html.

[27] *See* Interagency proposal, 84 Fed. Reg. at 24321 ("[F]oreign banking organizations often use U.S. branches to fund the larger global operations of the firm. For example, under the "funding branch" model, a foreign banking organization, via its U.S. branches, borrows in the U.S. wholesale funding markets to finance long-term, U.S. dollar-denominated project and trade finance around the world.").



(Source: Federal Reserve H.8)

In light of this shift, the perceived need to increase liquidity requirements at the IHC level to address liquidity risk at the branch level should be meaningfully mitigated.

Finally, the Federal Reserve already has the means to oversee liquidity at the U.S. branches and agencies of FBOs. Specifically, the Federal Reserve's Regulation YY provides a sufficient regulatory framework to address liquidity risk at the U.S. branches and agencies of FBOs. There is thus no need to impose more stringent liquidity requirements on the IHC to address what may be viewed, incorrectly, as a "gap" in the Federal Reserve's current ability to supervise and address liquidity risk at FBOs' U.S branches and agencies.[28]

B. If the agencies nevertheless implement a framework that would apply regulatory requirements to an FBO's IHC on the basis of characteristics of the FBO's CUSO, they should further tailor the application of the requirements to better reflect the IHC's actual risk profile.

As we detail above, the framework set forth in the proposals, which would apply certain requirements to the IHC on the basis of the CUSO (*i.e.*, on the basis of characteristics of entities and operations beyond those of the IHC itself), would result in the application of requirements to the IHC that may be a poor fit for the IHC's risk profile, creating significant regulatory and operational burdens without a corresponding supervisory benefit. If the agencies nevertheless implement this construct, the framework should be revised to mitigate the adverse consequences by further tailoring the CUSO-derived requirements that would apply to the IHC so that they better fit the IHC's actual risk profile.

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28 For similar reasons, there is no need to adopt a standardized liquidity framework that would apply to the U.S. branches and agencies of FBOs. See Section X below.

Specifically, if CUSO assets and risk-based indicators were used to determine the *applicability* of a requirement to the IHC, IHC assets and risk-based indicators should then be used to determine the *applicable tailoring* of that requirement. If, as a result of CUSO characteristics, the IHC were subject to a requirement that would not apply if applicability were determined on the basis of IHC characteristics alone, then the IHC-level requirement should be further tailored to be less stringent than currently proposed. For example, under the framework contemplated by the proposals, a Category IV IHC with less than $50 billion in wSTWF at the IHC level could be subject to the full LCR as a result of the CUSO having greater than $75 billion in wSTWF, but based on the IHC's own characteristics it should not be subject to the LCR at all. Under this scenario, the IHC should be subject to further tailored, less stringent LCR requirements (*e.g.*, a modified LCR and T+10 monthly FR 2052a reporting). This further tailoring of requirements applicable at the IHC level would alleviate regulatory and operational burdens that bear little relationship to the IHC's own characteristics.

C. Revising the proposals to account for the application of home-country standards to FBOs on a consolidated basis and the implications for IHC and CUSO liquidity could promote global cooperation and a global regulatory framework in which home-country and host-country requirements are more appropriately balanced.

As noted above in Section II.A.3, applying increased liquidity requirements and other enhanced prudential standards to the IHC on the basis of characteristics of the CUSO does not account for the mitigating effect of home-country standards and could result in increased misallocation risk and fragmentation, as well as, potentially, a collective action problem if other host jurisdictions react to the increased pre-positioning requirements in the United States by imposing similar requirements. Revising the proposals to eliminate this aspect and instead applying requirements to IHCs solely on the basis of their own characteristics would address these issues and could promote better global cooperation and home-host relationships.

Greater consideration of home-country standards would promote a balance of flexibility for home-country stakeholders, such as an FBO and its home-country supervisor, and certainty for local stakeholders, such as U.S. supervisors.[29] A framework that accounts for home-country standards and permits greater flexibility for FBOs (*i.e.*, by allowing the top of the group to allocate resources efficiently during periods of growth and stress) does not necessarily lead to reduced resiliency of the U.S. financial system. Indeed, greater consideration of home-country standards is likely to promote the resiliency of the U.S. financial system, while excessive pre-positioning of capital and liquidity resources within national borders could be detrimental to the overall resilience of financial institutions.[30] "[G]iven the uncertainty of the circumstances or location of losses that emerge in an actual stress, adequate flexibility for the parent to deploy resources where needed is likewise in the host regulator's interest."[31] Promoting global cooperation and a better balance between home-country and host-country requirements could also facilitate FBOs' continuing to provide credit to the U.S. economy and liquidity to U.S. capital markets.

Finally, U.S. regulatory requirements applicable to foreign-owned institutions may become a model for other jurisdictions.[32] If the U.S. imposes more stringent requirements on foreign-owned institutions and increases *ex-ante*

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[29] *See* Brand Your Cattle Speech.

[30] *See* FSB Report on Market Fragmentation, at 9.

[31] Brand Your Cattle Speech.

[32] *See id.* ("[W]illingness by the United States to reconsider its [internal TLAC] calibration may prompt other jurisdictions to do the same, which could better the prospects of successful resolution for both foreign G-SIBs operating in the United States, and for U.S. G-SIBs operating abroad.").

ring-fencing, other jurisdictions could take the same approach, which could have a negative impact on the agencies as home-country supervisors of U.S. organizations operating globally and on the global regulatory framework.[33]

III. The agencies should adopt the general framework of the risk-based indicator approach set forth in the proposals, subject to deploying it so that an IHC's characteristics determine IHC-level requirements, as discussed above, and to other important changes that would more appropriately tailor prudential requirements to the risk profiles of applicable FBOs.

Subject to the critical revision of applying IHC-level requirements and standards on the basis of the IHC's characteristics, we support the general framework the agencies have proposed to effect the tailoring of the application of enhanced prudential standards and the capital and liquidity requirements for the U.S. operations of FBOs. The risk-based indicator methodology underlying the proposals, if properly deployed, calibrated and indexed consistent with the recommendations described below, is a promising approach to implementing the tailoring intended by the agencies in issuing the proposals. We therefore encourage the agencies to adopt the general framework of the risk-based indicator approach as they proceed to implement EGRRCPA, and we make the following recommendations with respect to the risk-based indicator methodology.[34]

A. The wSTWF risk-based indicator should be changed in the final rules to exclude funding from affiliates and to more appropriately reflect underlying asset liquidity.

The wSTWF indicator has significant implications for the liquidity requirements that firms will be subject to under the revised framework. As proposed, the wSTWF metric overstates the risk of certain types of funding, resulting in the inappropriate application of more stringent liquidity requirements that are not commensurate with actual liquidity risk. wSTWF, as a liability-only measure, is problematic because the measure could lead to the imposition of inappropriate liquidity requirements based on relatively low-risk activities,[35] an issue that would be exacerbated if IHC-level requirements were determined on the basis of activities occurring within the FBO's U.S. branches and agencies.

1. Consistent with the cross-jurisdictional activity risk-based indicator, the final rules should exclude from the calculation of wSTWF funding from non-U.S. affiliates.

Under the proposals, wSTWF would be defined as the amount of funding obtained at the relevant organizational level of an FBO from wholesale counterparties or retail brokered deposits and sweeps with a remaining maturity of one year or less. In this measure, different categories of short-term wholesale funding would be weighted based on maturity, collateral (if any) backing the funding and counterparty characteristics. Unlike the cross-jurisdictional activity indicator, which would exclude all liabilities owed to non-U.S. affiliates, short-term funding

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33 *See id.* ("Our vantage point in the United States as a large home and host regulator would counsel that it is sensible to find a middle ground and fine tune our approach as we learn more and global conditions evolve.").

34 In addition to the specific recommendations described below, we note the lack of a conceptual link between single-counterparty credit limits and risk-based indicators other than size and off-balance-sheet foreign exposure. In this way, the proposed framework does not represent a holistic assessment of risk and could result in the application of more stringent standards (*e.g.*, more stringent single-counterparty credit limit requirements) on the basis of measures of risk unrelated to the standard (*e.g.*, wSTWF).

35 The issue of applying inappropriate requirements on the basis of low-risk assets and activities is also true of the nonbank asset indicator, discussed further in Section III.B.2 below.

from non-U.S. affiliates would be included in the wSTWF indicator because, according to the agencies, "reliance on [STWF] from affiliates can contribute to the funding vulnerability of [an FBO's] U.S. operations in times of stress."[36]

We strongly support exclusion of all liabilities owed to non-U.S. affiliates from the measure of cross-jurisdictional activity—indeed, this is consistent with a recommendation included in the BPI comment letter to the domestic tailoring proposals.[37] However, the rationale for excluding interaffiliate transactions from the cross-jurisdictional activities indicator applies with equal force to *all* of the risk-based indicators that will be used in the revised regulatory framework. Top-tier U.S. BHCs are required to eliminate transactions between the BHC and its consolidated subsidiaries when reporting on the FR Y-15 and other relevant Federal Reserve reporting forms, with the result being that intercompany transactions within the firm's consolidated operations, taken as a whole, are not counted towards the dollar-based thresholds in the reporting forms that inform the risk-based indicators set forth in the tailoring proposals.[38] FBOs, in contrast, would not be entitled to eliminate intercompany transactions between U.S. and non-U.S. affiliate entities, notwithstanding that all parties are consolidated under the parent FBO. Interaffiliate transactions are therefore treated very differently for the U.S. operations of FBOs compared to top-tier U.S. BHCs, with interaffiliate transactions for the U.S. operations of FBOs treated the same as third-party transactions. FBOs' interaffiliate transactions do not, however, present risks that make this treatment appropriate.[39]

As discussed above, FBOs have strong incentives to maintain funding at their U.S. operations, even during times of stress. A U.S. branch or agency is part of the foreign bank, and taking action to create (or omitting to take action to avoid) liquidity stress at part of the bank would not be in the bank's interest. With regard to subsidiary operations, FBOs have substantial investments in their U.S. subsidiaries and, where the IHC is subject to internal TLAC requirements, FBOs have effectively been required to cash collateralize support in the event of material financial distress affecting the IHC, which likewise provides a strong incentive for FBOs to support their subsidiary operations. The agencies' concern that reliance on short-term funding from non-U.S. affiliates can create funding vulnerabilities within U.S. operations is misplaced. The wSTWF indicator is intended to measure risks relating to potential funding runs, as, according to the agencies, "reliance on short-term, generally uninsured funding from more sophisticated counterparties can make those operations vulnerable to large-scale funding runs."[40] Interaffiliate

36 Federal Reserve proposal, 84 Fed. Reg. at 21998.

37 *See* BPI Domestic Tailoring Comment Letter, Section VI.B.

38 The instructions for the FR Y-15 provide, in relevant part, that all offices, including branches and subsidiaries, "that are within the scope of the consolidated holding company are to be reported on a consolidated basis. . . . As part of the consolidation process, the results of all transactions and all intercompany balances (e.g., outstanding asset/debt relationships) between offices, subsidiaries, and other entities included in the scope of the consolidated holding company are to be eliminated in the consolidation and must be excluded from the FR Y-15." Federal Reserve, Instructions for Preparation of Banking Organization Systemic Risk Report FR Y-15 (Dec. 2016) (the "**FR Y-15 Instructions**"), at GEN-1. The instructions for the FR Y-9C include analogous language. Federal Reserve, Instructions for Preparation of Consolidated Financial Statements for Holding Companies Reporting Form FR Y-9C (Sept. 2018), at GEN-4. The instructions for the FR Y-9LP provide, with respect to line item 17, that reporting holding companies should "[e]xclude balances due to subsidiaries and related institutions." Federal Reserve, Schedule PC to Instructions for Preparation of Parent Company Only Financial Statements for Large Holding Companies Reporting Form FR Y-9LP (March 2013), at PC-7.

39 *See* BPI Domestic Tailoring Comment Letter, Section VI.B. Although interaffiliate transactions should be excluded from the risk-based indicators, we strongly support the approach of treating transactions between the consolidated IHC and any affiliates (including the FBO's U.S. branches and agencies) in the same manner as transactions with third parties. *See* interagency proposal, at 84 Fed. Reg. 24319. Unlike the current construct in Section 252.157 of Regulation YY—which should be revised to permit internal and external cash flows to offset each other—the application of the LCR as described in the interagency proposal would not require an IHC to separately manage segregated net cash outflows involving affiliate and third-party transactions, which results in higher liquidity requirements than would otherwise be the case.

40 Interagency proposal, 84 Fed. Reg. at 24308.

funding—even if short-term and uninsured—does not present these or similar risks. During times of stress, affiliates are much more likely than third parties to roll over funding at maturity. Indeed, during times of stress, affiliate funding may replace third-party funding that may no longer be available. Further, certain interaffiliate short-term funding transactions are entered into as part of the global organization's internal risk management strategy and can be risk-reducing rather than risk-creating. It is therefore not appropriate to treat interaffiliate funding in the same manner as funding from third parties.

Accordingly, in order to subject the U.S. operations of FBOs to requirements that reflect their actual risk profiles, the final rules applicable to FBOs should explicitly carve out from the wSTWF indicator funding from affiliates. Carving out interaffiliate transactions from the wSTWF indicator would also address the different treatment accorded to U.S. firms and FBOs in the calculation of the indicator.

2. The agencies should revise the components of wSTWF to better reflect actual liquidity risk.[41]

As proposed, the wSTWF risk-based indicator overstates liquidity risk by failing to differentiate between sources of short-term funding based on their relative stability or risk profile. Examples of low-risk sources of short-term funding that should be carved out or otherwise re-measured to better reflect the actual liquidity risk profile include: insured affiliate-sourced brokered deposits (including sweep deposits), which generally exhibit balance permanence characteristics similar to retail and small business deposits, as well as draws on Federal Home Loan Bank and Federal Reserve Bank lines of credit, which are inherently low risk.

In addition to providing a more accurate picture of firms' risk profiles, revising the wSTWF risk-based indicator to better account for the relative stability and risk profile of different sources of funding, including by aligning the treatment for purposes of the revised framework with how these sources of funding are treated under other applicable regulations,[42] would promote consistency in regulation and could lessen compliance burdens for banking institutions.

3. The agencies should revise the components of wSTWF to take into account underlying asset liquidity.[43]

The components of wSTWF—specifically, those set forth in Schedule G and proposed new Schedule N to the Federal Reserve's Form FR Y-15—look only to the characteristics of liabilities and do not reflect underlying asset liquidity. Accordingly, the indicator should be revised to reflect the actual risks relating to an institution's use of short-term funding.

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41 Because the recommendations described in this section are generally applicable to both the proposals and the domestic tailoring proposals, the agencies should also reflect these changes in the final rules applicable to U.S. organizations.

42 For example, the LCR and proposed NSFR both recognize the relative stability of affiliate-sourced brokered deposits. The LCR assigns a 10% outflow rate to insured affiliate-sourced brokered deposit sweeps, and the proposed NSFR treats these deposits as longer-term funding with a relatively high 90% available stable funding factor. *See* 79 Fed. Reg. 61440, 61493 (Oct. 10, 2014); 81 Fed. Reg. 35124, 35157 (June 1, 2016). In addition, with respect to affiliate-sourced brokered deposits (including sweep deposits), this source of funding also does not present the funding-run risk that the agencies cite in the interagency proposals because affiliates are less likely than third parties to withdraw their support or change funding arrangements. Indeed, affiliate funding may be used to replace third-party funding that has been withdrawn in times of stress.

43 Because the recommendations described in this section are generally applicable to both the proposals and the domestic tailoring proposals, the agencies should also reflect these changes in the final rules applicable to U.S. organizations.

According to the agencies, FBOs "that fund long-term assets with short-term liabilities from financial intermediaries such as investment funds may need to rapidly sell less liquid assets to meet withdrawals and maintain their operations in a time of stress, which they may be able to do only at 'fire sale' prices."[44] By looking only at the characteristics of liabilities, the proposed wSTWF indicator would not measure whether an FBO's funding presents these risks. For example, an institution may finance certain of its HQLA, such as U.S. Treasuries, with short-term funding. If the institution's counterparty did not roll its funding, the characteristics of the underlying assets—here, U.S. Treasuries—would mitigate liquidity risk for the FBO, as well as the risk of a "fire sale" that could have broader implications for the U.S. financial system. Short-term funding may also be used as part of a prudent risk management strategy to offset short-term assets that are low-risk (such as reverse repurchase agreements) and/or result from financial institutions' crucial role in the market (such as balances "due to" in supply chain finance). Further, an institution may mitigate liquidity risk relating to short-term funding by maintaining balances at a Federal Reserve Bank. By looking only at the characteristics of liabilities without considering the tenor, liquidity and other relevant characteristics of the assets funded by those liabilities, the wSTWF indicator as proposed does not provide an accurate measure of liquidity risk.

Due to the significant implications the wSTWF indicator has for the liquidity requirements that firms will be subject to under the revised framework, it is imperative that the wSTWF indicator be calculated in a way that more appropriately reflects actual risks associated with the use of short-term funding. Looking at only the characteristics of funding without accounting for underlying asset liquidity provides an incomplete picture of liquidity risk and should not be the basis for the application of more stringent liquidity requirements.

4. Risks relating to the use of short-term funding are already mitigated significantly by liquidity requirements applicable to FBOs on a global, consolidated basis under home-country regulations and by sources of funding available to IHCs.

The preamble to the Federal Reserve proposal describes the perceived risks posed by short-term wholesale funding in the FBO context, stating that "many [FBOs rely] on short-term wholesale funding obtained in the United States to fund their global investment activities" and that such funding models present "unique vulnerabilities." The Federal Reserve attributes FBOs' "disproportionate use of dollar-denominated short-term wholesale funding" to the fact that U.S. branches of FBOs generally lack access to retail deposits, which is characterized as a more stable source of funding. However, this view of FBOs' funding activities and the resultant risk should not be the basis of applying more stringent liquidity requirements with respect to an IHC. First, as explained in Section II.A.5 above, the borrowing/lending profiles of U.S. branches of foreign banks have shifted significantly since 2011, with U.S. branches providing a significant source of funding to the U.S. credit markets such that there is an overall net "due to" foreign-owned branches operating in the United States. Second, there are a number of mitigating factors to the potential risks relating to FBOs' use of short-term funding, including the underlying asset liquidity described above and the existing liquidity risk management and liquidity buffer requirements in Regulation YY, as well as the fact that FBOs maintain HQLA in order to satisfy home-country LCR requirements that apply on a global, consolidated basis. Third, as noted above, IHCs can—and many do—have insured depository institutions that have access to retail deposits as a source of funding, which further illustrates the disconnect between the perceived problem (the use of wholesale funding by an FBO's U.S. branches and agencies) and the proposed solution (more stringent liquidity requirements with respect to the FBO's IHC).

The changes to the wSTWF indicator we have proposed would address our concerns with the proposed formulation without resulting in any increased risk to the U.S. financial system.

44 Interagency proposal, 84 Fed. Reg. at 24308.

B. The nonbank assets risk-based indicator should be reformulated to exclude assets that represent claims on affiliates and to better account for actual risks presented by various types of assets currently deemed to be "nonbank assets" under the proposals.

The "nonbank assets" metric is infrequently used in the bank regulatory framework. Prior to the tailoring proposals, the metric had been used in the Federal Reserve's capital plan rule[45] and the Federal Reserve's and FDIC's resolution planning rule.[46] The metric is not well developed and, as discussed below, it is not indicative of risk. The agencies should therefore significantly revise the proposed nonbank assets indicator so that it is risk-sensitive and can further—rather than frustrate—the tailoring of prudential requirements to the risk profiles of various firms.

1. Consistent with the cross-jurisdictional activity risk-based indicator, the final rules should exclude from the calculation of nonbank assets those assets which represent claims on affiliates.

As explained in Section III.A.1 above, the rationale for excluding interaffiliate transactions from the cross-jurisdictional activities indicator applies with equal force to *all* of the risk-based indicators that will be used in the revised regulatory framework, including the nonbank assets indicator. Nonbank assets that represent claims on affiliates are not indicative of interconnectedness and a heightened risk profile. Rather, many affiliate-related nonbank assets are risk-reducing because the underlying interaffiliate transactions—such as interaffiliate loans and derivatives transactions—often relate to risk management transactions and strategies.

2. The agencies should revise the definition of "nonbank assets" in the final rules to better account for the actual underlying risks of the activities conducted in nonbank subsidiaries.[47]

The definition of "nonbank assets" would capture certain low-risk or no-risk assets that are not indicative of a heightened risk profile. As we have previously argued, firms should not be subject to more stringent standards because they hold low-risk or no-risk assets, including bank-permissible assets, in nonbank entities.[48] Holding such assets in nonbank entities is not necessarily indicative of a heightened risk profile that would make it appropriate to subject firms to more stringent capital or liquidity requirements. The agencies assert that "[n]onbank activities may involve a broader range of risks than those associated with banking activities,"[49] but the proposed nonbank assets indicator would not take into account whether nonbank assets relate to bank-permissible activities, in which case this rationale for the nonbank assets indicator would not apply. Further, the nonbank assets indicator would not reflect the actual underlying risks of the activities an FBO conducts in nonbank subsidiaries. All activities in a nonbank entity—regardless of risk—would be treated the same way, based on the gross balance sheet impact. The agencies

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45 12 C.F.R. § 225.8.

46 12 C.F.R. Part 243 (Federal Reserve) and Part 381 (FDIC).

47 Because the recommendations described in this section are generally applicable to both the proposals and the domestic tailoring proposals, the agencies should also reflect these changes in the final rules applicable to U.S. organizations.

48 *See, e.g.*, The Clearing House, *Comment Letter re: Amendments to the Capital Plan and Stress Test Rules* (Docket No. R-1548; RIN 7100 AE-59) (Nov. 23, 2016) (arguing that firms should not be deemed "large and complex" because they hold bank-permissible assets in nonbank subsidiaries and pointing out that the $75 billion nonbank asset threshold identified in the proposal was selected without empirical support).

49 Interagency proposal, 84 Fed. Reg. at 24307.

also assert, without offering empirical support, that "banking organizations with significant investments in nonbank subsidiaries are more likely to have complex corporate structures and funding relationships, and substantial inter-affiliate transactions that can add operational challenges."[50] The proposed nonbank assets indicator would not, however, measure the complexity of an organization's corporate structure or its funding transactions, or the extent to which any of its transactions might lead to operational challenges. Rather, the indicator would measure the amount of assets held in nonbank entities without differentiating among the assets based on the risks of those assets or the activities in connection with which the assets are held.

To be more risk sensitive, nonbank assets should be subject to weighting on the basis of risk, as is the case for the treatment of certain collateralized funding in the wSTWF indicator, to better reflect actual risks presented. For example, a significant portion of the underlying assets (such as U.S. Treasuries) are in fact bank-permissible, highly liquid and very low risk. A gross measure of nonbank assets is not indicative of risk—assigning weights to assets for purposes of calculating this risk-based indicator would create a regulatory framework in which a more risk-sensitive measure determines whether firms become subject to more stringent capital, liquidity and other prudential requirements.

3. Risks relating to nonbank activities are already mitigated significantly by liquidity and other requirements, including resolution planning requirements, applicable to FBOs on a global, consolidated basis under home-country regulations.

Consistent with our earlier arguments, we note that the concerns raised by the agencies regarding FBOs' nonbank activities are already mitigated by existing regulatory requirements, including those applicable to the FBOs on a global, consolidated basis under home-country regulations. In addition, in the preamble to the Federal Reserve proposal, the Federal Reserve observed that "some [FBOs] engage in complex activities through broker-dealers in the United States, which are highly interconnected to U.S. and foreign financial intermediaries… The crisis experience demonstrated that nonbank activities could exacerbate the effects of a banking organization's distress or failure, due to the business and operational complexities associated with these activities." To the extent there are concerns about the business and operational complexities associated with nonbank activities, those are best addressed through regulatory requirements regarding operational continuity and resolution planning. The proposals do not take into account the existence or effectiveness of home-country requirements, or how changes in FBOs' operational continuity and resolution planning capabilities since the financial crisis address—as a result of both home-country requirements and the Federal Reserve's and FDIC's resolution planning requirements—the agencies' concerns regarding the experiences from the financial crisis.

C. The cross-jurisdictional activity risk-based indicator should be revised in the final rules to exclude all transactions with non-U.S. affiliates and to exclude certain other transactions and exposures that are not indicative of a heightened risk profile.

Under the framework created by the proposals, crossing the $75 billion threshold for cross-jurisdictional activities would subject firms to some of the most stringent standards applicable to banking organizations operating in the United States. It is therefore critical that the cross-jurisdictional activities risk-based indicator accurately measure whether or not the firm has a sufficiently heightened risk profile such that those stringent standards are appropriately applied. The following recommendations would better tie the indicator to the actual risks presented by firms' activities:

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50 *Id.* at 24307.

- With respect to FBOs and consistent with the reasons set forth in Sections III.A.1 and III.B.1 above, the cross-jurisdictional activities risk-based indicator should exclude *all* interaffiliate transactions, including all interaffiliate claims.[51]

- With respect to both FBOs and U.S. firms, reverse repurchase agreements involving domestic Level 1 HQLA (such as U.S. Treasuries) with both affiliates and non-affiliates should not be characterized as "cross-jurisdictional." Because of the nature of the collateral, these transactions are low risk and not indicative of cross-jurisdictional activity.

- With respect to both FBOs and U.S. firms, the cross-jurisdictional activities risk-based indicator should exclude liabilities to and claims against home-country and host-country sovereigns (including political subdivisions) and supranational, international and regional organizations (such as the World Bank). With respect to such sovereign exposures, these may result from formal or informal regulatory requirements (including LCR requirements), and, in any event, are not indicative of complexity or interconnectedness that would make the imposition of Category II standards necessary or appropriate. As a general matter, these types of exposures present limited credit risk and many have a zero risk weight or are exempt from restrictions under other regulations (*e.g.*, the Volcker Rule).

- With respect to both FBOs and U.S. firms, the cross-jurisdictional activities risk-based indicator should exclude delivery-versus-payment transaction "trade date" receivable amounts on the basis that they are low risk and, as relevant to FBOs, would be unlikely to qualify as collateralized exposure under the proposals.[52]

- With respect to both FBOs and U.S. firms and consistent with the reasons set forth in Sections III.A.3 above, the cross-jurisdictional activities risk-based indicator should be adjusted to better account for underlying asset liquidity for purposes of calculating outstanding cross-jurisdictional liabilities.

D. The off-balance-sheet exposures risk-based indicator should be adjusted in the final rules to better account for FBO organizational structures and to incorporate risk-sensitive measures.

The agencies should adjust the off-balance-sheet exposures risk-based indicator so that FBOs' U.S. operations are treated analogously to U.S. BHCs. At the very least, the calculation of the off-balance-sheet exposures risk-based indicator for the CUSO should exclude intra-entity transactions and activities. The off-balance-sheet exposures risk-based indicator should also exclude potential future exposures ("PFEs") associated with affiliate derivatives clearing activities so long as the relevant affiliate complies with ongoing margin requirements. The exclusion of PFEs under these circumstances is in accordance with the central clearing objectives of both the Dodd-Frank Act and post-crisis derivatives reforms that have been adopted in non-U.S. jurisdictions.

In addition, the off-balance-sheet exposure risk-based indicator should be reformulated for all firms to be more risk-sensitive by assigning risk weights to different types of exposures in accordance with their risks to the individual firm. For example, loan commitments, letters of credit and guarantees used in corporate finance transactions should be assigned lower weights relative to other types of off-balance-sheet exposures because of the relatively low risks associated with these exposures. Further, any off-balance-sheet line of credit that cannot be

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51 Cross-jurisdictional activities with respect to the CUSO should, at the very least, exclude all transactions that occur within the same legal entity but happen to cross geographic boundaries.

52 See Annex A, Section V for additional information.

drawn unless it is collateralized should be treated as a collateralized transaction, with permitted netting of the exposure against the amount of collateral required.

E. The agencies should not subject banking organizations to Category II standards on the basis of meeting a higher threshold for one or more of wSTWF, nonbank assets and off-balance-sheet exposures.

The proposals seek comment on whether, in addition to the proposed asset size and cross-jurisdictional activity thresholds, Category II standards should apply to firms based on wSTWF, nonbank assets and off-balance-sheet exposures, using a higher threshold than the $75 billion threshold that would apply for Category III standards.[53] For the reasons set forth below, the agencies should not subject banking organizations to Category II standards based on these additional risk-based indicators.

The introduction of additional risk-based indicators, each one of which could cause a firm to be subject to Category II standards, would exacerbate existing flaws with the proposed Category II boundaries. As discussed in the BPI domestic tailoring comment letter, a quantitative analysis supports the conclusion that the $75 billion cross-jurisdictional activity threshold should be significantly increased, and this conclusion is bolstered by a number of policy and economic reasons for promoting cross-border borrowing practices.[54] That comment letter also pointed out that subjecting firms to the stringent standards of Category II[55] on the basis of crossing a single threshold (either total consolidated assets or cross-jurisdictional activities) was counter to the tailoring directives set forth in EGRRCPA.[56] Adding additional indicators, any one of which could result in a firm being placed in Category II, only aggravates this disconnect.

Category II requirements are intended to apply to those firms that are "very large or have significant international activity"[57] and therefore subject to the Basel standards applicable to very large or complex firms.[58] Adding the new risk-based indicators, as suggested by the agencies, would not facilitate the identification of firms that fit this description. Nonbank assets and wSTWF do not measure whether a firm is "very large" or has "significant international activity" and, although off-balance-sheet exposure is conceptually linked to size, it does not on its own identify whether a firm is "very large" or has "significant international activity." Subjecting firms to Category II standards as a result of crossing a threshold set for any one of these risk-based indicators is therefore inappropriate. Similarly, firms should not be subject to Category II liquidity requirements—specifically, full LCR, full NSFR and daily FR 2052a reporting requirements—if they have $75 billion or more in wSTWF but would not otherwise be subject to Category II standards, as is currently proposed for both U.S. and non-U.S. firms. The imposition of such stringent

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53 Interagency proposal, 84 Fed. Reg. at 24308; Federal Reserve proposal, 84 Fed. Reg. at 21998.

54 *See* BPI Domestic Tailoring Comment Letter, Section II.A. As noted in the BPI domestic tailoring comment letter, it is desirable for banking organizations to diversify their funding sources. Cross-border funding can mitigate creditor concentrations and does not *a priori* present significant risks, as firms have expertise in managing foreign exchange risk. In addition, raising local funding is a sound asset-liability management and risk-management practice. Finally, cross-border borrowing can be less expensive than other forms of funding.

55 Federal Reserve proposal, 84 Fed. Reg. at 21992 (noting that requirements under Category II generally would remain unchanged from existing requirements).

56 *See* BPI Domestic Tailoring Comment Letter, Section II.D.

57 Federal Reserve domestic tailoring proposal, 83 Fed. Reg. 61408, 61410; Interagency domestic tailoring proposal, 83 Fed. Reg. 66024, 66027.

58 Federal Reserve proposal, 84 Fed. Reg. at 22002.

regulatory requirements based on crossing a single threshold that does not appropriately measure liquidity risk could result in the application of regulatory requirements that are a poor fit for the subject institution. Moreover, those requirements should only apply to firms that are very large or internationally active and, in the case of daily FR 2052a reporting, should only apply to systemically important firms.[59]

Although we do not support subjecting firms to Category II standards on the basis of additional risk-based indicators, we recognize that the agencies are actively considering this approach, including what would be appropriate thresholds for each additional risk-based indicator.[60] Accordingly, if the agencies nevertheless determine that wSTWF, nonbank assets and/or off-balance-sheet exposures should be included as additional indicators that would place firms in Category II, the threshold for these indicators with respect to Category II should be no less than $210 billion[61] to (i) maintain proportional parity among the indicators for different categories under the framework; (ii) avoid negative implications for the availability of credit and participation by FBOs in U.S. markets; and (iii) maintain the overall integrity of the categories and the framework proposed by the agencies. We discuss each of these in turn below.

Under the tailoring proposals, a Category IV firm would become a Category III firm if it has either $250 billion in total consolidated assets or $75 billion in wSTWF, nonbank assets or off-balance-sheet exposures, while a Category III firm would become a Category II firm if it has either $700 billion in total consolidated assets or $75 billion in cross-jurisdictional activities. The asset threshold for the Category II boundary is therefore 2.8x the asset threshold for the Category III boundary. If wSTWF, nonbank assets or off-balance-sheet exposures are to be included as indicators defining the Category II boundary, this same multiple (2.8x) should be used to adjust the current $75 billion threshold for the risk-based indicators that place firms in Category III.[62] This would maintain proportional parity among the indicators for different categories under the framework.

In addition, setting the threshold for new Category II risk-based indicators at a lower threshold (*i.e.*, placing more firms in Category II) could impair the ability of banking organizations to meet the credit needs of businesses, consumers and local governments and, as discussed in Section II.4 above, could discourage FBOs from participating in the U.S. market as a result of being subject to increasingly stringent U.S. regulatory standards. Setting another, relatively low threshold on these risk-based indicators could have negative implications for how organizations manage their growth, inhibiting the provision of credit to borrowers through attempts to minimize off-balance-sheet exposures[63] and creating disincentives for prudent risk management procedures associated with certain types of wSTWF.[64] Placing firms in Category II on the basis of crossing a relatively low threshold for nonbank assets, which

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59 *See also* Section V.A; BPI Domestic Tailoring Comment Letter, Section IV.B.

60 *See* Interagency proposal, 84 Fed. Reg. at 24308; Federal Reserve proposal, 84 Fed. Reg. at 21998.

61 Consistent with Section III.F, any dollar threshold should be indexed to the growth of total assets of commercial banks in the United States.

62 For example, a firm with $700 billion in total assets and $210 billion in wSTWF would have the same ratio of wSTWF to total assets (2.8x) as a $250 billion asset firm with $75 billion in wSTWF. In other words, the *relative reliance* of the two firms on wSTWF would be the same.

63 For many Category III and Category IV banks, off-balance-sheet exposures mainly consist of traditional lines of credit extended to corporate customers and local governments, as well as lines of credit (such as home equity lines and credit cards) to consumers.

64 See Section III.A.3.

as proposed would capture certain low-risk or no-risk assets that are not indicative of a heightened risk profile,[65] could also further reduce the presence of FBOs in the U.S. capital markets.

Finally, setting relatively low thresholds for new risk-based indicators that would place firms in Category II would inappropriately widen the pool of firms subject to the most stringent regulatory standards in the United States—a pool that should be limited to those organizations with very large and complex operations that the agencies have stated would be subject to standards consistent with those developed by the Basel Committee on Banking Supervision and should be further limited with respect to daily 2052a reporting requirements. We see no reason to broadly expand the universe of firms subject to these standards on the basis of crossing relatively low thresholds for risk-based indicators such as wSTWF, nonbank assets and off-balance-sheet exposures, particularly when the underlying assets and liabilities making up each of these indicators, as proposed, do not reliably predict a heightened risk profile.[66]

F. The final rules should provide for annual adjustments to the dollar thresholds used to assign firms to different categories to account for economic growth by indexing these dollar thresholds to the growth in domestic banking assets.

We reiterate the recommendation in the BPI domestic tailoring comment letter that the final rules applicable to domestic and foreign firms *must* provide for annual adjustments to the dollar thresholds used to assign firms to different categories in order to account for economic growth.[67] Annual adjustments can be achieved by indexing the dollar thresholds set forth in the domestic tailoring proposals and the proposals to the growth in domestic banking assets, as published in the Federal Reserve's H.8 statistical release, Assets and Liabilities of Commercial Banks in the United States.

Over time, firms' asset size and risk-based indicators may increase as their activities expand in response to growth in the banking sector and the economy more generally. If a firm's asset size and risk-based indicators increase proportionately to increases in domestic banking assets, the firm's relative significance and risk profile within the U.S. banking system—as measured by the framework set forth in the domestic and foreign tailoring proposals—generally remains static even though the absolute value of its assets or risk-based indicators is increasing. Those increases would reflect the expansion of the banking sector and the economy more generally, not changes in the firm's risk profile. If, in contrast, a firm's asset size or risk-based indicators increase disproportionately to increases in domestic banking assets, the firm's relative U.S. risk profile—as measured by the framework set forth in the tailoring proposals—may be changing such that a different category within the framework created by the proposals could be more appropriate. Annual adjustments to the dollar amount of the risk-based indicators and $700 billion asset size threshold for Category II[68] based on changes in domestic banking assets would help prevent the application of more

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65 See Section III.B.2.

66 As described in Sections III.A.3 and III.B.2, each of the wSTWF and nonbank assets indicators, as proposed, capture low-risk or no-risk assets and do not properly account for underlying liquidity and the execution of sound risk management strategies. In addition, for many Category III and Category IV firms, off-balance-sheet exposures mainly consist of traditional lines of credit, and firms should not be subject to the most stringent regulatory requirements on the basis of traditional lending activities that are not indicative of being "very large" or having "significant international activity."

67 *See* BPI Domestic Tailoring Comment Letter, Section II.B.

68 The rationale for adjusting the $700 billion asset threshold for Category II applies equally well to the $100 billion and $250 billion asset thresholds for Category IV and Category III, respectively. However, we recognize that the $100 billion and $250 billion asset thresholds are used to maintain consistency between the proposals and EGRRCPA, which includes these thresholds, but did not provide for indexation of these amounts.

stringent capital, liquidity and other prudential standards to firms simply because the banking sector in general has grown. To promote transparency and certainty regarding the application of regulatory standards, the final rules should provide that the adjustments occur automatically based on the availability of data on domestic banking assets.

G. Recommendations with respect to the risk-based indicator framework set forth in the BPI domestic tailoring comment letter also apply to the framework set forth in the proposals.

The BPI domestic tailoring comment letter included several recommendations with respect to the risk-based indicator approach proposed for large U.S. institutions which are equally applicable to the proposals and should be reflected in the final tailoring rules for FBOs.[69] Specifically:

- The dollar-based threshold for cross-jurisdictional activity should be significantly increased (or, at a minimum, if the $75 billion threshold is retained, cross-jurisdictional liabilities should be excluded), both because of the conclusions drawn from the BPI quantitative analysis summarized in the domestic tailoring comment letter and for a number of policy and economic reasons described in Section II.A of the domestic tailoring comment letter.

- The agencies should clearly identify in the preambles to the final rules the line items in the applicable reporting forms for the risk-based indicators.

- The agencies should not subject FBOs and their U.S. subsidiaries to Category II requirements on the basis of meeting any single indicator threshold, whether on the basis of the $700 billion asset threshold or the $75 billion cross-jurisdictional activities threshold.

IV. The final rules should incorporate transition periods for those FBOs that would be subject to more stringent requirements, including single-counterparty credit limits and certain reporting obligations, as a result of the revised framework.

Due to the changes the proposals would make to the applicability of LCR requirements, certain FBOs not currently subject to the LCR rule with respect to their IHCs would become subject to LCR requirements, and, with respect to certain IHCs currently subject to the modified LCR, the applicable LCR requirements would become more stringent. The agencies would provide "initial transition periods" for FBOs to comply with LCR and NSFR requirements with respect to their IHCs and for covered depository institution subsidiaries to comply with LCR and NSFR requirements. These periods would depend on whether a firm is subject to the requirements as of the effective date of a final rule, and which requirements apply to it as of the effective date. However, the proposals would also result in increased compliance burdens for certain FBOs with respect to other aspects of the regulatory framework, and the agencies should incorporate into the final rules transition periods within which FBOs can come into compliance with new or more stringent requirements.

Specifically, with respect to single-counterparty credit limits, the revisions set forth in the proposals would increase the compliance burdens currently applicable to certain IHCs with less than $250 billion in assets.[70] In addition, certain firms would become subject to more stringent reporting requirements, such as accelerated FR 2052a reporting requirements (notably, an increase from monthly to daily reporting for some firms and a migration from a T+10 monthly submission to a T+2 monthly submission for others), as a result of the changes in the proposals. In order to provide FBOs with sufficient time to conform to previously inapplicable standards, the final

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[69] *See* BPI Domestic Tailoring Comment Letter, Sections II.A, II.C, and II.D.

[70] Federal Reserve proposal, 84 Fed. Reg. at 22004.

rules should include appropriate transition periods consistent with the approach taken for the application of new or more stringent LCR requirements.

V. The recommendations with respect to the capital and liquidity frameworks set forth in the BPI domestic tailoring comment letter also apply to the frameworks set forth in the proposals.

A. The agencies should revise the liquidity framework in the final rules applicable to FBOs consistent with our recommendations to the domestic tailoring proposals.

The BPI domestic tailoring comment letter included several recommendations with respect to the liquidity framework proposed for large U.S. institutions which are equally applicable to the proposals and should be reflected in the final tailoring rules for FBOs.[71] Specifically:

- The agencies should use the modified LCR and proposed modified NSFR to develop the less stringent LCR and NSFR (if retained)[72] requirements for qualifying Category III firms rather than subjecting those firms to a new "reduced" LCR or NSFR requirement.[73]

- The Federal Reserve should not expand the universe of firms subject to daily FR 2052a reporting requirements.

- For Category IV firms, the Federal Reserve should explicitly confirm that Category IV firms would not be subject to any LCR-based requirements or supervisory expectations as a result of any continuing FR 2052a reporting obligations and should take steps to appropriately reduce reporting burdens for those firms.

B. The agencies should revise the capital framework in the final rules applicable to FBOs consistent with our recommendations to the domestic tailoring proposals.

The BPI domestic tailoring comment letter included several recommendations with respect to the capital framework proposed for large U.S. institutions which are equally applicable to the proposals and should be reflected in the final tailoring rules for FBOs.[74] Specifically:

- The Federal Reserve should confirm that the internal capital stress test required of Category III firms during the "off" year would be fully aligned with existing CCAR and DFAST stress testing requirements,

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71 *See* BPI Domestic Tailoring Comment Letter, Section IV.

72 BPI has previously questioned the basis for and utility of the NSFR. *See* Bill Nelson, *Six questions about the Net Stable Funding Ratio (NSFR) requirement* (Sept. 21, 2018), *available at* https://bpi.com/six-questions-about-the-net-stable-funding-ratio-nsfr-requirement/.

73 Before subjecting FBOs' U.S. operations to the NSFR (if adopted), the agencies must conduct an impact analysis assessing the potential impact of the NSFR on IHCs. In connection with the proposal of the NSFR rule, the agencies conducted an impact analysis of covered companies that did not include IHCs, because the proposal predated the IHC requirement. *See* 81 Fed. Reg. 35124, 35161 (June 1, 2016). The impact analysis assessing the potential impact of the NSFR to IHCs should take into account that the FBO parent would also be subject to the NSFR so that any form of the NSFR ultimately applied to the IHC appropriately balances home- and host-country requirements.

74 *See* BPI Domestic Tailoring Comment Letter, Sections III.D, III.F and III.G.

but with only the capital action assumptions applicable in CCAR and without the public disclosure required under DFAST.

- The forward-looking analysis previewed for Category IV firms in the domestic tailoring proposals should not be applied in a manner that would continue to require these firms to run hypothetical stress scenarios.

- The capital plan proposal to be issued by the Federal Reserve should codify key aspects of the guidance that has been provided through the CCAR and DFAST Questions and Answers.

VI. The Federal Reserve should revise the stress testing requirements under the capital plan rule to provide meaningful relief for Category III firms during the "off" year of the DFAST stress testing cycle.[75]

The proposals create relief for Category III firms by reducing the requirement to complete and publish the results of company-run stress tests (DFAST) from annual to every other year, such that there is an "off year" when companies are not required to run these stress tests. However, under the Federal Reserve's capital plan rule, these firms continue to be required to run stress tests under both supervisory and internal scenarios on an annual basis. In order for the relief created by the proposals with respect to DFAST requirements to be meaningful, during the off year, Category III firms should only be required to run stress tests under a single internal scenario for capital plan rule purposes. This would facilitate the Federal Reserve's continuing annual review of such firms' capital plans under stressed scenarios and would relieve the time pressure associated with the need to wait for supervisory scenarios to be released before the models can be run.

VII. The agencies should not create a $50 billion wSTWF threshold that would subject both domestic and foreign Category IV firms to more stringent liquidity requirements.

The domestic tailoring proposals, when initially released, did not apply LCR or NSFR requirements to Category IV firms. However, in developing the proposals, the Federal Reserve determined that "some domestic or foreign banking organizations that meet the criteria for Criteria IV standards could potentially have a heightened liquidity risk profile," for example, if they are not funded by "stable deposits" or if they materially rely on less-stable STWF and therefore lack "traditional balance sheet structures."[76] The proposals therefore, with respect to an IHC, would apply reduced monthly LCR and proposed NSFR requirements as Category IV standards if the CUSO has $50 billion or more of wSTWF. The agencies also re-proposed this aspect of the domestic tailoring proposals to create an analogous requirement for covered Category IV firms.

The final rules should not create a $50 billion wSTWF threshold that would subject Category IV firms to more stringent liquidity requirements. Instead, the agencies should adopt a framework that is consistent with that initially proposed for large domestic firms—that is, a framework that does not apply reduced LCR or proposed NSFR requirements to Category IV firms. The stated rationale for the proposed change—and the acknowledgement that no U.S. banking organization would currently satisfy these criteria[77]—suggests that it is designed to target a specific

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75 Because the recommendations described in this section are generally applicable to both the proposals and the domestic tailoring proposals, the agencies should also reflect these changes in the final rules applicable to U.S. organizations.

76 Interagency proposal, 84 Fed. Reg. at 24316.

77 Federal Reserve Staff Memorandum re Notices of proposed rulemaking to align prudential standards for foreign banking organizations with those proposed for domestic banking organizations (April 1, 2019), *available at* https://www.federalreserve.gov/aboutthefed/boardmeetings/files/foreign-bank-board-memo-20190408.pdf.

foreign firm or small number of foreign firms. Concerns about a specific firm or small number of firms are more appropriately addressed through supervision than through broadly applicable regulation. Addressing institution-specific concerns through added regulatory requirements that are codified in the regulatory framework also undermines the policy goal of promoting simplicity in regulation.

VIII. FBOs should not be required to report for the CUSO data unrelated to the risk-based indicator framework set forth in the proposals.

In order to implement the aspects of the proposals that would determine the applicable requirements on the basis of the characteristics of an FBO's CUSO, the Federal Reserve proposal would modify the FR Y-15 to require FBOs to report data for their CUSO that are related to the criteria for determining applicable categories under the proposals. The proposed changes to the FR Y-15 are, however, broader than necessary to implement the proposal because the changes would generally replicate Schedules A–G for FBOs' CUSO, including with respect to reporting requirements that relate to the Federal Reserve's GSIB surcharge rule but not the risk-based indicators underlying the proposals. The Federal Reserve should limit the data required to be reported for the CUSO to only those data that are necessary to calculate the risk-based indicators used to assign FBOs to different categories under the regulatory framework. For example, FBOs should not be required to report for the CUSO (1) any of the data required by proposed Schedule J—FBO Substitutability Indicators or (2) the average risk-weighted assets required by line item 7 of proposed Schedule N—FBO Short-Term Wholesale Funding Indicator. Both proposed Schedule J and line item 7 of proposed Schedule N relate to information that domestic bank holding companies report for purposes of calculating their GSIB scores. This information is not related to the calculation of any of the risk-based indicators underlying the proposed regulatory framework. Requiring FBOs to report data relating to the substitutability category in the GSIB surcharge framework or average risk-weighted assets would result in the imposition of significant and undue burdens on FBOs, as they are not currently required to track or report this information on a CUSO basis, and the reporting of such information would not further a supervisory purpose. The expansion of reporting requirements applicable to, and on the basis of, the CUSO should not be broader than necessary to implement the proposals.

IX. The Federal Reserve should revise the definition of "highly liquid assets" in Regulation YY to expressly include HQLA under the LCR.

The Federal Reserve requests comment on whether to "more closely align the assets that qualify as highly liquid assets" for the purposes of the liquid asset buffer requirements of Regulation YY with "HQLA under the current LCR rule."[78] The existing internal, company-designed liquidity stress testing requirements under Regulation YY and the standardized, supervisor-designed LCR rule together create a robust and complementary liquidity stress testing and risk measurement framework. These two liquidity requirements serve two different purposes: one a uniform benchmark of liquidity adequacy (the LCR), the other an internal measure of idiosyncratic risk (Regulation YY). Thus, any substantive changes to the definition of highly liquid assets should preserve and enhance the complementary aspects of the current liquidity stress testing framework.

We support greater alignment between the definitions of HQLA and "highly liquid assets" and recommend that the Federal Reserve revise the definition of "highly liquid assets" under Regulation YY to expressly include HQLA without any obligation on the part of the firm that it "demonstrate" that the inclusion of HQLA is appropriate for this purpose. As the Federal Reserve noted in the release adopting enhanced prudential standards for U.S. BHCs and FBOs, HQLA should generally qualify as "highly liquid,"[79] and codifying this view in an amendment to Regulation YY would promote the policy goals of fairness and effectiveness in regulation by permitting firms to treat HQLA in a

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78 Federal Reserve proposal, 84 Fed. Reg. at 22007.

79 79 Fed. Reg. 17240, 17259 (March 27, 2014).

manner consistent with the Federal Reserve's own view without undertaking to make the demonstration currently required by Regulation YY.[80]

Notwithstanding the foregoing recommendations, it is critical to keep internal liquidity stress tests and related buffer requirements distinct from the LCR requirement. Liquidity stress testing frameworks are set by each organization to reflect the organization's own view of its liquidity risk and broader risk profile, and are tailored to its particular activities and balance sheet composition. On the other hand, the LCR is a standardized measure of liquidity adequacy that provides regulators a uniform view of organizations' liquidity risk and a single metric to compare across organizations. Keeping these requirements distinct creates a diversity of liquidity risk measurement tools and facilitates organizations' management of their liquidity against a more robust overall liquidity framework.

To that end, when implementing this suggested revision, the Federal Reserve should retain the catch-all prong of the highly liquid asset definition in Regulation YY to "provide[] companies discretion to determine whether an asset would be liquid under a particular scenario"[81] for purposes of the liquidity stress testing requirements, which are tailored to the individual company's liquidity profile.[82] Retention of this prong in the definition of highly liquid assets would appropriately reflect that the LCR is a standardized requirement but the Regulation YY liquidity buffer requirement is not.

Likewise, for purposes of including HQLA in the definition of highly liquid assets, the Federal Reserve should exclude the haircuts and concentration limits assigned in the LCR because, unlike the liquidity stress testing requirements of Regulation YY, the LCR is a "standardized measure of liquidity adequacy" that facilitates a "comparison across covered companies" rather than a "a view of an individual firm under multiple scenarios."[83] Applying the haircut and concentration framework of the LCR to highly liquid assets for Regulation YY purposes could prevent an organization from establishing approaches tailored to its specific risks, effectively turning the Regulation YY liquidity stress testing and buffer framework into a uniform standard rather than a tailored and distinct risk management and supervisory tool. Further, if restrictions and underlying assumptions for highly liquid assets matched those for HQLA, then, to meet liquidity requirements, organizations would be pressured to align corresponding stress outflow assumptions with the standardized ones provided in the LCR rule. The result would not be an organization's view of its liquidity positions or a view of how stressed liquidity outflows would be tailored to the organization's risk profile. The diversification and haircut requirements in Regulation YY are sufficient to achieve the Federal Reserve's supervisory objectives and are appropriate in light of the differences between the standardized LCR and the Regulation YY requirements. Accordingly, those Regulation YY requirements should not be changed.

X. The agencies should not impose standardized liquidity requirements on FBOs with respect to their U.S. branch and agency networks.

In addition to seeking comment on the revised regulatory framework set forth in the proposals, the agencies also seek comment on whether they should impose standardized liquidity requirements—such as an LCR-based requirement—on the U.S. branches and agencies of FBOs. The application of any such requirements would be subject to a separate notice-and-comment rulemaking.

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80 12 C.F.R. § 252.157(c)(7)(i)(C).

81 79 Fed. Reg. 61440, 61466 (Oct. 10, 2014).

82 *Id.* at 61466.

83 *Id.* at 61466.

As appropriately recognized, the imposition of standardized liquidity requirements to the U.S. branches and agencies of FBOs would be "novel in the realm of international regulation (in contrast to supervision, where there is precedent)."[84] Although we accept that any such requirements must be the subject of "robust public discourse—domestically and internationally—on its advantages and disadvantages,"[85] we believe that, at least at this time, the disadvantages are so compelling that the issue should not be further considered. We are at a crucial point in establishing the global regulatory framework for U.S. and foreign banks that operate internationally. As the agencies consider the creation of an entirely new regulatory requirement, we urge them to consider whether an international bank should be subject to regulatory requirements that are duplicative of those applied at a consolidated level in each host country where it operates. Imposition of branch liquidity requirements would represent a significant step in creating such a duplicate framework.

Consistent with our arguments in Section II above, in light of (1) complementary home- and host-country regulatory requirements, including the significant bolstering of FBO resiliency as a result of the post-crisis framework, (2) FBOs' strong incentives to maintain adequate support for their U.S. branch and agency networks and (3) the Federal Reserve's existing regulations and supervisory tools addressing U.S. branch liquidity through Regulation YY requirements, FBOs' U.S. branches and agencies do not present liquidity risk that would justify the imposition of an entirely new regime regulating U.S. branch and agency liquidity. To the extent the agencies determine that additional measures are needed to address any perceived risks to the U.S. financial system resulting from the liquidity risk at FBOs' U.S. branches and agencies, rather than impose an entirely new regime that could have unwanted cascading effects (discussed below), as alternatives, the agencies should consider whether there are other approaches that would better address liquidity risks relating to FBOs' U.S. branches and agencies, such as enhanced supervisory procedures and central bank-to-central bank funding lines or discounted host-country liquidity requirements.[86]

The expansion in host-country supervision represented by a standardized liquidity framework applicable to FBOs' U.S. branches and agencies could result in increased stringency of liquidity requirements applicable to the foreign operations of large domestic firms if other jurisdictions were to adopt a similar framework. This could have multiple negative effects: (1) domestic firms would be put in a worse competitive position with respect to operations abroad and would also have less flexibility to allocate resources efficiently based on business opportunities, (2) the resultant increase in pre-positioning of resources would reduce resources available in the United States in the event of resolution of a large domestic firm and (3) the resultant increase in pre-positioning worldwide as a result of the collective action problem (described in Section II.A.3 above). Ultimately, such an approach could lead to global ring-fencing that would undermine the resiliency of the global financial system.

XI. The agencies should address in the final rules certain technical matters related to the reporting forms underlying the regulatory framework.

Technical matters are addressed in Annex A of this letter.

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84 Vice Chair for Supervision Randal K. Quarles, *Opening Statement on Proposals to Modify Enhanced Prudential Standards for Foreign Banks and to Modify Resolution Plan Requirements for Domestic and Foreign Banks* (Apr. 8, 2019), *available at* https://www.federalreserve.gov/newsevents/pressreleases/99A5C407E998418CB2CB9DDB85C54B0B.htm#aboutMenu.

85 *Id.*

86 For example, the Federal Reserve could eliminate Regulation YY liquidity requirements with respect to U.S. branches and instead impose a discounted LCR (*e.g.*, 65% or 75%).

The Bank Policy Institute and the American Bankers Association appreciate the opportunity to comment on the proposals.

Respectfully submitted,

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Annex A: Technical Matters

We propose the following changes to the Federal Reserve's FR Y-15.[1]

I. Reporting of new information by branches will take time for firms to operationalize and implement and should be accompanied by appropriate transition periods while firms build out these capabilities in their reporting structures.[2]

- Issue: Many of the proposed changes to the FR Y-15 will require FBOs to report data on behalf of their U.S. branches that are not currently required to be reported and which will require the buildout of new technology to accommodate.
  - For example, the data required by proposed Schedule H—FBO Size Indicator are not currently reported by FBOs for their U.S. branches, and FBOs will require time to build the reporting of these data into their existing systems.
  - The Federal Reserve appropriately recognized that transitioning firms to full reporting requirements would facilitate firms' compliance with FRY Y-15 reporting requirements when the report was first adopted in December 2012. Specifically:
    - For a firm's initial FR Y-15 submission, firms were permitted to rely on "reasonable estimates" for data reported, including for purposes of the chief financial officer attestation requirement.[3]
    - Firms were given 90 days, rather than 60 days, to submit the first FR Y-15 report based on annual data.[4]
    - For the first several years after the adoption of the FR Y-15, firms were only required to report data on an annual (rather than quarterly) basis.[5]
    - For Schedule G—Short-Term Wholesale Funding Indicator, reporting requirements were phased in from December 31, 2016 through June 30, 2018 based on whether the reporting

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[1] *See generally* Federal Reserve proposal, 84 Fed. Reg. at 22009–22010; Federal Reserve, Reporting Forms, Data Collections Currently under Review by the Board of Governors of the Federal Reserve System, *available at* https://www.federalreserve.gov/apps/reportforms/review.aspx.

[2] Consistent with Section VIII of this comment letter, we reiterate that FBOs should not be required to report for the CUSO data unrelated to the risk-based indicator framework set forth in the proposals. For example, FBOs should not be required to report for the CUSO (1) any of the data required by proposed Schedule J—FBO Substitutability Indicators or (2) the average risk-weighted assets required by line item 7 of proposed Schedule N—FBO Short-Term Wholesale Funding Indicator, as both relate to information that domestic bank holding companies report for purposes of calculating their GSIB scores and do not relate to the calculation of any of the risk-based indicators underlying the proposed regulatory framework.

[3] 77 Fed. Reg. 76484, 76486 (Dec. 28, 2012).

[4] *Id.* at 76484. Today, firms have 65 days to submit the FR Y-15 based on annual data. FR Y-15 Instructions, at GEN-2 (explaining that quarterly reporting requirement became effective starting with the June 30, 2016 as-of date).

[5] *See* FR Y-15 Instructions, at GEN-2 (explaining that quarterly reporting requirement became effective starting with the June 30, 2016 as-of date).

firms were GSIBs, non-GSIB advanced approaches firms or other firms with at least $50 billion in assets.[6]

- Recommendation: Changes to the FR Y-15 that will require firms to adjust their current practices and build new technology into their operating systems should be accompanied by appropriate transition periods. At a minimum, for new CUSO reporting obligations, the Federal Reserve should provide transition provisions similar to those that were applicable to firms when the FR Y-15 report was first adopted.

II. Further changes to the instructions are needed to account for the obligation to report data on behalf of the CUSO.

- Issue: The proposed instructions have not been revised to fully account for FBOs' reporting of CUSO data. For example, references to the FFIEC 009 are not accompanied by analogous references to the FFIEC 019, and references to the FR Y-9C are not accompanied by analogous references to the FFIEC 002.[7]

- Recommendation: Correct throughout the instructions the cross-references to other reporting forms in order to account for the inclusion of data related to branch and agency operations. These revisions would promote efficiency and simplicity in the reporting process by eliminating interpretive issues.

III. FBOs should be permitted to use "spot" data to calculate the size indicator under Schedule H unless the FBO's IHC is required to calculate average data due to its status of being subject to the supplementary leverage ratio.

- Issue: The proposed instructions to Schedule H replace "advanced approaches banking organizations" with "Category II and III FBOs."[8]

  - For Category II or III FBOs, on-balance sheet items would be reported using daily averages and off-balance sheet items would be reported using monthly averages.[9] FBOs assigned to Category IV and below would be permitted to use either "spot" or averages for all data required to be reported.[10]

    - As assigned categories for the FBO's CUSO and IHC may differ, some IHCs currently filing FR Y-15 reports as non-advanced approaches firms not subject to supplementary leverage ratio requirements may be forced to move from spot to average calculations based on the FBO's CUSO, imposing a significant operational burden on the IHC even if the IHC is subject to Category IV capital standards.

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6 *See* FR Y-15 Instructions, at G-1.

7 *See* Federal Reserve, Draft Instructions for Preparation of Systemic Risk Report FR Y-15 (Apr. 2019) (the "**Draft FR Y-15 Instructions**"), *available at* https://www.federalreserve.gov/reportforms/formsreview/FR_Y-15%20Instruction%20Revisions%20(FBO%20Tailoring)%20Final.pdf.

8 *Id.* at H-1–H-6.

9 *Id.* at H-1.

10 *Id.* at H-1.

- The proposed framework is circular in that reporting requirements for Schedule H would depend on the results reported in Schedule H.

➢ Recommendation: Permit an FBO to use quarter-end calculations for the CUSO unless it has an IHC that is required to use average calculations as a result of being subject to the supplementary leverage ratio. Daily averages are most relevant for capital requirements, such as the supplementary leverage ratio, which do not apply to the non-IHC portion of the CUSO, so there is no need to require an FBO to calculate daily averages for its CUSO if it does not have an IHC subject to the supplementary leverage ratio.

IV. The Federal Reserve should clarify ambiguity in the General Instructions as to the application of netting of payable and receivable amounts from foreign affiliates.

➢ Issue: The General Instructions would define rules of consolidation for foreign banking organizations to be reported across Columns A, B and C (U.S. branches and agencies, the IHC and the CUSO, respectively) in each of Schedules H–N.[11] The instructions would provide for the netting of gross due to/due from balances with affiliates.[12]

- Because these instructions would apply to multiple schedules and subsections, including the calculation of wSTWF, nonbank assets and off-balance-sheet exposures, it is not clear if the netting instructions would apply solely to funding transactions or to any line item in any schedule.

- If netting were permitted for all line items, it is not clear how the netting should be effected if the gross due to/due from captures differences in both amount and tenor. For example, in calculating wSTWF under Schedule N, it is not clear how the netting should apply if there are receivables and payables against the same affiliate in different reporting tiers/tenors.

➢ Recommendation: Clarify whether affiliate netting can be applied to all line items on each of Schedules H–N, including items other than total on-balance sheet assets, and if so, clarify the principles for application of such netting.

V. The calculation of the cross-jurisdictional activity risk-based indicator should not include delivery-versus-payment ("DVP") transaction "trade date" receivable amounts.

➢ Issue: The Federal Reserve proposal seeks comment on (1) "the most appropriate way in which the proposed cross jurisdictional activity indicator could account for the risk of transactions with a delayed settlement date" and (2) "the advantages and disadvantages of the use of settlement date accounting versus trade-date accounting for purposes of the cross jurisdictional activity indicator."[13]

- When acting in a primary dealer capacity or otherwise providing access to U.S. markets to non-U.S. affiliates and/or customers, an FBO's broker-dealer subsidiary will routinely incur "trade date" receivables on its balance sheet when selling U.S. securities to non-U.S. parties.[14]

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11 *Id.* at GEN-2.

12 *Id.* at GEN-2.

13 Federal Reserve proposal, 84 Fed. Reg. at 21996.

14 We note that such receivables have low risk profiles and are therefore treated favorably under the U.S. Basel III and LCR rules.

    - Under the current FFIEC 009 instructions, no risk transfer can be applied to the trade date receivable. Further, under the Federal Reserve proposal, the receivable would be unlikely to qualify as collateralized exposure and would therefore be counted dollar-for-dollar toward the cross-jurisdictional activity risk-based indicator.

- The transactions in question are executed on a DVP basis, often referencing U.S. Treasuries settling on T+1. The risk associated with the trades is capped at the mark-to-market changes between the trade and the settlement date, which is often immaterial in light of the volatility of the securities and the length of the settlement period.

    - The characteristics of the transaction make it inappropriate to treat the full amount of the trade date receivable as cross-jurisdictional activity for purposes of the risk-based-indicator framework.

- It may not be feasible for an FBO-owned broker-dealer to move to settlement date accounting even under circumstances in which such an option were permitted and would result in a benefit with respect to the calculation of the FBO's cross-jurisdictional activities.

➢ Recommendation: Exclude DVP transactions' trade date receivable amounts from cross-jurisdictional activity calculations or explicitly allow for a risk transfer/collateral haircut approach to the calculation.

VI. The final rules and/or the FR Y-15 should clarify ambiguity in the interagency proposal with respect to the treatment of exposures to securities lending agreements and repurchase agreements with third parties for purposes of calculating cross-jurisdictional activities.

➢ Issue: The interagency proposal notes two ways in which the calculation of cross-jurisdictional activities under the proposal would differ from the FFIEC 009, one of which is that the proposal would require allocation of exposures to securities lending agreements and repurchase agreements on an ultimate-risk basis (subject to netting), rather than solely on the basis of the residence of the counterparty.[15]

➢ The above statement is made in connection with a discussion of the treatment of affiliate claims. It is therefore not clear if the intention is to require ultimate risk reporting for claims related to both third-party and affiliate securities lending agreements and repurchase agreements.

➢ Recommendation: Confirm that ultimate risk reporting will be required for claims related to both third-party and affiliate securities lending agreements and repurchase agreements.

VII. The Federal Reserve should clarify Schedule H to cure an ambiguity with respect to cash and collateral posted to versus received from counterparties in derivative transactions.

➢ Issue: Line item 1(e) of Schedule H provides that FBOs should "[r]eport the amount of qualifying cash variation margin, which is posted to a counterparty to a derivative contract and included in item 3(a) as an on-balance sheet receivable."[16] However, Line item 3(a) provides that FBOs should "[i]nclude the amount of on-balance sheet cash and collateral received from counterparties in derivative

15 Interagency proposal, 84 Fed. Reg. at 24305 n.57.

16 Draft FR Y-15 Instructions at H-2.

transactions."[17] Line item 1(e) thus refers to a receivable (collateral posted) while Line Item 3(a) refers to a payable amount (collateral received).

- Recommendation: Clarify whether line item 3(a) should reference a receivable balance (collateral pledged) similar to item 1(e).

[17] *Id.* at H-4.