June 16, 2025

Via Electronic Mail

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Moody's Ratings

Re: Banks: Moody's Ratings Proposed Methodology Update

Ladies and Gentlemen:

The Bank Policy Institute[1] appreciates the opportunity to comment on the proposed changes to the rating methodology applicable to banks published by Moody's Ratings on April 30, 2025.

I. Introduction

We broadly support a bank rating methodology that is transparent, appropriately designed and calibrated, and capable of providing comparable ratings in light of the significant differences in regulatory requirements, business models, balance sheet structures, accounting practices and public disclosures among banks across and within jurisdictions. However, we are concerned that the proposed changes would not achieve that objective.

For capital, the proposed changes are insufficiently explained and conceptually flawed, and would introduce further opacity in ratings. For liquidity, the proposed calibration of the Liquid Resources sub-factor is too high. In addition, by using liquidity coverage ratio ("LCR") concepts, the proposed changes would broadly apply regulatory constructs designed for, and applicable to, only a subset of banks to determine the ratings of every bank—including those not subject to the LCR at all—which raises challenges regarding consistency and comparability of the framework. And, despite substantial differences in interest rate risk modeling and risk management practices among banks, the proposed changes would rely on

[1] The Bank Policy Institute is a nonpartisan public policy, research and advocacy group that represents universal banks, regional banks, and the major foreign banks doing business in the United States. The Institute produces academic research and analysis on regulatory and monetary policy topics, analyzes and comments on proposed regulations, and represents the financial services industry with respect to cybersecurity, fraud, and other information security issues.

banks' interest rate risk disclosures to assign ratings, which would result in inconsistent application of the proposed bank rating methodology.

These issues would be compounded by the increased reliance in the methodology on qualitative adjustments that would be available for Moody's to impose. In many cases, the scope and rationale for the proposed additional qualitative adjustments are opaque and based on faulty or unexplained assumptions, which could raise the risk of inconsistent application and conflicts with the broader objectives to enhance the clarity of these adjustments. We are concerned that volatility in the underlying quantitative metrics in the proposed framework, including the incorporation of the buffer framework, could lead to further reliance on these qualitative adjustments.

It is critical for any revised bank rating methodology to have objective and transparent standards that can be applied consistently across banks of all sizes and business models given the overall importance of ratings for banks and their investors, depositors, other funding providers, counterparties and customers. We have described in this letter several thematic observations and concerns, along with suggestions to enhance any revisions to Moody's bank ratings methodology.

II. Capital

In broad terms, the proposed changes relating to the capital sub-factor would require banks to hold additional capital in order to maintain their current ratings under the existing Moody's framework. Despite this significant change to the framework, the proposal does not adequately justify the rationale for the increased calibration. In fact, from a U.S. perspective, current bank capital levels are close to the upper end of recent academic studies on optimal capital levels.[2] Moreover, the Federal Reserve indicated in its most recent Supervision and Regulation Report that "most banks continued to report capital levels well above applicable regulatory requirements".[3] In particular, the Federal Reserve noted that large banks are "well positioned to weather the severe recession they were tested against and stay above minimum capital requirements" and banks "with less than $100 billion in total assets also continued to report strong regulatory capital levels."[4]

In testimony before the Senate Banking Committee and House Financial Services Committee in February 2025, Federal Reserve Chair Powell similarly noted that the level of capital in the banking system for the largest banks is about right. Relatedly, several principals at the U.S. federal banking agencies have suggested "capital neutrality" as a potential starting place for revisions to the capital framework to implement Basel III Endgame.[5] The Moody's proposal itself also recognizes "the substantial growth in

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[2] See Letter from the Bank Policy Institute and the American Bankers Association to Ann E. Misback, Secretary of the Board of Governors of the Federal Reserve System, James P. Sheesley, Assistant Executive Secretary of the Federal Deposit Insurance Corporation and the Chief Counsel's Office of the Office of the Comptroller of the Currency, *Regulatory Capital Rule: Large Banking Organizations and Banking Organizations with Significant Trading Activity*, pp. 18-20 (Jan. 16, 2024), *available at* https://bpi.com/wp-content/uploads/2024/01/ABA-BPI-Basel-III-Endgame-Comment-Letter-Final-2024.01.16.pdf.

[3] Federal Reserve, *Supervision and Regulation Report*, p. 3 (Nov. 2024), *available at* https://www.federalreserve.gov/publications/files/202411-supervision-and-regulation-report.pdf.

[4] Federal Reserve, *Supervision and Regulation Report*, p. 3.

[5] Federal Reserve Governor Michelle W. Bowman, *The Path Forward for Bank Capital Reform* (Jan. 17, 2024), *available at* https://www.federalreserve.gov/newsevents/speech/bowman20240117a.htm (noting that the original Basel III Endgame proposal "far exceeds" the Basel standards and that "policymakers must develop

banks' capitalization over the last decade."[6] However, the proposed changes do not adequately reflect this current strength of banks or explain why, despite current capital levels, capital must be higher for banks to maintain their ratings. The Moody's bank rating methodology should not effectively require higher capital for banks to maintain their current ratings given the already very high levels of bank capital, the widespread recognition that there is more than ample capital in the banking system and the clear trajectory of regulatory capital requirements.

A. The proposed updates to the TCE/RWA ratio and buffer thresholds should not be implemented.

The higher capital calibration would result, in part, from the proposed recalibration of the tangible common equity ("TCE") to risk-weighted assets ("RWA") ratio, setting the lowest category at below 7%, in contrast to "around 5% in the current methodology."[7] Moody's states that this increase reflects "our view that a higher point of failure more closely aligns with the capital levels at which banks have failed, or at which regulators have stepped in over the last decade."[8] Moody's also explains that it views "the minimum capital requirement to be around 7%, reflecting the minimum requirements for common equity, mandatory buffers applied for countercyclicality and systemic importance, additions for interest rate risk, and supplementary requirements imposed by supervisors including those resulting from stress tests or a formal review process."[9] In addition, under the proposal, Moody's would be "unlikely to assign a sub-factor score above that indicated by the financial ratio category of Moderate where a bank holds an excess of capital less than 1.5% of RWA above its minimum regulatory requirements[, and w]here the excess is below 1%, we are unlikely to assign a sub-factor score above that indicated by the financial ratio category of Weak."[10]

First, there is insufficient support to increase the TCE/RWA ratio bands in the manner proposed. With respect to a 7% TCE/RWA ratio representing a new point of nonviability, the 2023 banking stress does not support the underlying premise in the proposal that regulators have sought to resolve banks at incrementally higher capital levels. Silicon Valley Bank and First Republic Bank had TCE/RWA ratios substantially in excess of 7% at the time of their respective failures. The failure of Credit Suisse, similarly, was not related to its TCE/RWA ratio, let alone whether that ratio was closer to 7% than 5%. Despite the idiosyncratic factors underlying the 2023 banking stress, for which TCE/RWA ratios were not a relevant factor, the proposal would subject all banks under the Moody's framework to higher capital requirements, as measured by the TCE/RWA metric, to maintain their current ratings in respect of the capital sub-factor,

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and work toward a target, a top-line aggregate capital level that would best promote safety and soundness and one that has a broad consensus among policymakers. Earlier efforts on the Basel proposal would have resulted in something closer to 'capital neutrality'—with essentially minimal top-line change in aggregate capital requirements across the U.S. banking system."); FDIC Vice Chairman Travis Hill, *Charting a New Course: Preliminary Thoughts on FDIC Policy Issues* (Jan. 10, 2025), *available at* https://www.fdic.gov/news/speeches/2025/charting-new-course-preliminary-thoughts-fdic-policy-issues ("I continue to believe that a proposal that is *roughly* capital neutral, consistent with the original objectives of U.S. and international regulators, remains a prudent starting point.") (footnote text omitted).

6 Proposal, p. 2.

7 Proposal, p. 2.

8 Proposal, p. 2.

9 Proposal, p. 31.

10 Proposal, p. 31.

despite no underlying changes imposed by the banking agencies. The proposed changes to the TCE/RWA ratio also lack conceptual coherence. The point of nonviability would be treated as being higher (now 7%, vs. 5% before), yet there is no recognition that, all else equal, if a bank has more capital at the time of failure, there is a larger cushion to absorb losses.

Similarly, there is no justification provided for the incorporation of a buffer framework into the proposed revisions, which would compound the issue of banks holding management buffers in excess of the regulatory buffers that, in turn, are on top of the minimum regulatory requirements. Moody's indicates that it "consider[s] the minimum capital requirement to be around 7%," which reflects a number of elements beyond the 4.5% minimum common equity Tier 1 capital requirement in the Basel framework.[11] In other words, the 7% "minimum capital requirement" considered by Moody's and underpinning the revised TCE/RWA ratio calibration already reflects that there are regulatory buffers on top of the minimum regulatory requirements. Indeed, when the Basel Committee calibrated the 4.5% minimum capital requirement, it noted that "the regulatory minimum requirement is the amount of capital needed for a bank to be regarded as a viable going concern by creditors and counterparties."[12] Under that logic, Moody's incorporation of a buffer into its rating methodology could result in the Basel Committee further raising minimum requirements, leading to an endless upward spiral of capital requirements.

The proposed approach also would be inconsistent with investor expectations and the manner in which banks deploy management buffers on top of regulatory buffers. The level of bank management buffers broadly varies across banks and individual banks may shift these buffers upward or downward over time for a variety of idiosyncratic or macroeconomic reasons. A rating methodology that imposes a uniform buffer requirement across banks and market conditions would not be appropriate.

Adjusting the score downward if a bank's excess capital is below 1% of RWA also is at odds with the capital conservation buffer framework and associated limitations when the buffer is not satisfied in full and could create unnecessary ratings volatility that would be detrimental to fixed income investors. Conceptually, the capital conservation buffer framework in the U.S. permits banks to continue to engage in lending and other intermediation activities to support the economy when the buffer is not satisfied in full. In these circumstances, banks are permitted to engage in certain capital distributions or discretionary bonus payments, so long as those are permitted under the applicable payout ratio limitations. In fact, during the COVID crisis, as they have during other periods of market stress, the U.S. banking agencies encouraged banking organizations "to use their capital and liquid buffers as they respond to the challenges presented by the effects of the coronavirus", noting that the buffers "were designed to provide banking organizations with the means to support the economy in adverse situations and allow banking organization to continue to serve households and businesses."[13] A rating methodology that penalizes banks for merely approaching the buffer is entirely inconsistent with this framework, fails to take into account that there can be a variety of reasons a bank decides to deploy its buffer and could have undue procyclical effects during periods of stress.

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11 Proposal, p. 31.

12 Basel Committee, *Calibrating regulatory minimum capital requirements and capital buffers: a top-down approach*, p. 1 (Oct. 2010), *available at* https://www.bis.org/publ/bcbs180.pdf.

13 Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, *Statement on the Use of Capital and Liquidity Buffers* (Mar. 17, 2020), *available at* https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20200317a1.pdf.

These concerns are compounded by the opacity, volatility and foundational flaws of the current capital conservation framework in the U.S. For banks subject to the stress capital buffer ("SCB") requirement, the capital conservation buffer requirement for purposes of the standardized approach is equal to its SCB requirement plus any applicable countercyclical capital buffer ("CCyB") amount. For global systemically important banks ("GSIBs"), the capital conservation buffer also includes the GSIB surcharge in addition to the SCB and CCyB.

With respect to the SCB, the Federal Reserve issued a proposed rule in April 2025 that "would help to reduce volatility of the stress capital buffer requirements."[14] The Federal Reserve further acknowledged that "[d]ue to the changing hypothetical nature of the test, the results also change and introduce volatility each year."[15] The Federal Reserve has also indicated that, by September 30, 2025, it expects to request comment on its stress test models and scenarios.[16] In the midst of an acknowledgement from the Federal Reserve that it is revising the stress testing framework to reduce volatility and increase transparency, it is not appropriate for the Moody's bank methodology to implement, effectively, an additional buffer requirement on top of the SCB given the substantial issues with the current SCB framework, including its year-over-year volatility and determination through the use of models and scenarios that do not benefit from the public notice-and-comment process. There are similar issues with respect to banks that are subject to the GSIB surcharge, particularly given the well documented, punitive nature of the U.S.-specific Method 2 calculation.[17] Under the proposed methodology, GSIBs would need to hold an additional buffer inclusive of the SCB requirement and GSIB surcharge to avoid a lower sub-factor score, resulting in further inconsistencies in the application of Moody's methodology across banks.

B. There is insufficient support for the 30% threshold applicable to the unrealized losses to TCE ratio, which would also increase the opacity of the methodology.

The proposal provides that Moody's would be "likely to adjust the [Capital] sub-factor score downward by one or more notches" when the level of unrealized losses represents 30% or more of TCE or where these losses rise "sharply" within a period of a year or less.[18]

There is no empirical justification provided for the 30% threshold, which would introduce significant cliff effects. More broadly, this adjustment would not appropriately reflect the differences in accounting treatment for different types of securities and loans and the different regulatory requirements that apply to banks. Notably, the extent of unrealized losses of any individual bank recognized in TCE would depend on the bank's accounting classifications, in particular as available-for-sale ("AFS") or held-to-

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14 Federal Reserve, *Modifications to the Capital Plan Rule and Stress Capital Buffer Requirement*, 90 Fed. Reg. 16,843 (Apr. 22, 2025).

15 Federal Reserve, *Federal Reserve Board requests comment on a proposal to reduce the volatility of the capital requirements stemming from the Board's annual stress test results* (Apr. 17, 2025), *available at* https://www.federalreserve.gov/newsevents/pressreleases/bcreg20250417a.htm.

16 Bank Policy Institute et. al. v. Board of Governors of the Federal Reserve System, *Joint Motion To Stay Proceedings*, Case No. 2:24-cv-04300 (filed May 23, 2025), *available at* https://bpi.com/wp-content/uploads/2025/05/Joint-Motion-to-Stay-Proceedings-2025.05.23.pdf.

17 Sean Campbell, Francisco Covas and Guowei Zhang, *The Federal Reserve Should Revise the U.S. GSIB Surcharge Methodology to Reflect Real Risks and Support the Economy* (Oct. 11, 2023), *available at* https://bpi.com/the-federal-reserve-should-revise-the-u-s-gsib-surcharge-methodology-to-reflect-real-risks-and-support-the-economy/.

18 Proposal, p. 32.

maturity ("HTM") for securities. In general, HTM securities are carried at amortized cost for balance sheet purposes, whereas AFS securities are carried at fair value with unrealized gains or losses recorded in accumulated other comprehensive income. The proposed methodology does not specifically address these different accounting classifications and their effect on the unrealized losses to TCE ratio metric.

In addition, in the U.S., banks subject to Category I and Category II standards already are required to recognize unrealized losses on AFS securities in regulatory capital. As a result, for these banks, unrealized losses on AFS securities would affect both the unrealized losses to TCE ratio and the application of the additional buffer requirement addressed above. Incorporating the unrealized losses to TCE metric into Moody's ratings methodology, accordingly, would create further inconsistencies when comparing the rating methodology metrics across banks. The proposed changes do not address this potential duplicative and punitive treatment of unrealized losses on AFS securities.

Moody's states that the level of any downward adjustment "would reflect the magnitude of the unrealized losses, the expected duration of the loss position, the source of the unrealized losses and the likelihood that such losses would be realized."[19] But the proposal does not include any objective framework for assessing these factors, making it impossible to discern how they might be applied, particularly in a consistent way across banks. Additionally, even if this type of adjustment were to remain in the revised methodology, it would be inconsistent and result in asymmetric treatment to not provide for any corresponding upward adjustment for banks with low levels of unrealized losses relative to TCE.

C. The RWA density metric is ill-suited for comparison for banks within a jurisdiction and across business models.

The proposal would use "the ratio of RWA to tangible assets to estimate or calculate RWA density" and adjust "the sub-factor score based on whether this ratio is above or below the median for the rated universe of banks."[20] Under the proposed methodology, Moody's would adjust the TCE/RWA score upward based on a directionally higher RWA/tangible assets ratio and lower in the case of a lower RWA/tangible assets ratio, as reflected in Exhibit 18.[21] The stated rationale for this adjustment is based on "greater consistency in assessing the effect of nominal leverage on a bank's capital strength" and "reducing the effects of some of the unwarranted differentiation in calculating risk weights between banks adopting the standardized approach and those using internal rating-based models, as well as between the variations in approach across jurisdictions."[22]

In addition to the lack of justification supporting the calibration of the RWA density figures provided in the grid in Exhibit 18, the proposal, more fundamentally, does not sufficiently justify incorporating a RWA density metric into the methodology. Although the proposal suggests the RWA density is intended to permit comparisons of banks across jurisdictions, the RWA density calculation is not a meaningful measure of a bank's leverage and is particularly inappropriate for differentiating the creditworthiness of banks within a particular jurisdiction subject to the same standards, especially, as is the case in the U.S., when all banks are required to apply a standardized, non-modeled approach in calculating RWAs. Moody's states that the RWA density metric is designed to capture a bank's nominal leverage,

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19 Proposal, p. 32.

20 Proposal, p. 2.

21 Proposal, p. 31.

22 Proposal, pp. 2-3.

without explaining why this metric is more fit for purpose than an ***actual*** leverage metric comparing a measure of capital to the bank's balance sheet.[23] Even if the RWA density metric were an appropriate measure of bank leverage, the proposal would place undue emphasis on this metric given that, in general, leverage ratios are intended as a "backstop measure" to risk-based capital requirements.[24]

Moreover, the RWA density metric would lead to illogical results and would introduce significant variability in calibration across banks, particularly for certain business models. Although a higher ratio of RWAs to tangible assets generally would seem to indicate a bank's assets are riskier (all else equal), the proposed calibration would in fact assume that a higher ratio indicates a bank's probability of failure is lower. Under that approach, assets with zero risk weights (including Reserve Bank balances and U.S. Treasuries) would be treated as incrementally risky.

In that regard, banks engaged in significant custody and trust activities would be penalized for holding substantial levels of assets with a 0% risk-weight, including U.S. Treasuries and balances at a central bank. Banks engaged in Treasury intermediation activities would be penalized for holding Treasury securities in inventory. Similarly, to the extent that a bank holds a greater level of assets with very low risk-weights, including high-quality liquid assets ("HQLA") required under the liquidity framework, the bank's RWA density metric would in fact be worse under the proposal, while its Liquid Resources metric (core banking liquidity to tangible banking assets) would improve, an illogical result. An activity—encouraged by regulation—would simultaneously be treated as both promoting and detracting from the bank's creditworthiness. This also would be inconsistent with recent comments from several principals at the U.S. federal banking agencies regarding potential proposed amendments to the leverage ratio framework, including to address constraints on the ability of banks to intermediate in U.S. Treasury markets.[25]

III. Liquidity and Funding Structure

A. The Liquid Resources sub-factor is over-calibrated and does not appropriately reflect HQLA held at subsidiaries.

The proposal would use the ratio of core banking liquidity to tangible banking assets to assess a bank's liquidity quality.[26] The calibration of this core banking liquidity to tangible banking assets ratio in the grid in Exhibit 22 is too high and insufficient justification is provided for the removal of non-HQLA from the numerator while largely maintaining the existing denominator and related thresholds. Notably, the core banking liquidity metric would reflect HQLA at the consolidated level of the top-tier entity and would not appropriately reflect HQLA held at subsidiaries. Because bank holding companies generally would not

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[23] Proposal, pp. 2-3.

[24] Board of Governors of the Federal Reserve System, OCC, *Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Capital Adequacy, Transition Provisions, Prompt Corrective Action, Standardized Approach for Risk-weighted Assets, Market Discipline and Disclosure Requirements, Advanced Approaches Risk-Based Capital Rule, and Market Risk Capital Rule*, 78 Fed. Reg. 62,018, 62,031 (Oct. 11, 2013) (referring to the Basel III leverage ratio as "a backstop measure to the risk-based capital requirements").

[25] See, e.g., Federal Reserve Governor Michelle W. Bowman, *Bank Regulation in 2025 and Beyond* (Feb. 5, 2025), *available at* https://www.federalreserve.gov/newsevents/speech/bowman20250205a.htm; Federal Deposit Insurance Corporation Acting Chairman Travis Hill, *View from the FDIC: Update on Key Policy Issues* (Apr. 8, 2025), *available at* https://www.fdic.gov/news/speeches/2025/view-fdic-update-key-policy-issues.

[26] Proposal, p. 40.

count HQLA at a depository institution subsidiary in excess of the subsidiary's projected net cash outflows, the LCR at the level of the consolidated bank holding company is not an appropriate measure of liquidity.[27]

The proposal broadly provides that "core banking liquidity already excludes trapped liquidity" and that "depending on where a subsidiary is located, HQLA may exclude a portion of the subsidiary's liquidity that we may view as available in times of stress", in which case Moody's may adjust the Liquid Resources sub-factor upward.[28] However, the methodology for making any of these upward adjustments is not clearly specified in the proposal. We are concerned that these adjustments may not be applied consistently across banks and will understate bank levels of HQLA, particularly given that, for many bank holding companies, the depository institution represents a significant proportion of the holding company's consolidated outflows and excess HQLA.

B. The overreliance in the Liquidity and Funding Structure on LCR metrics raises comparability concerns.

The proposal would introduce changes to the Funding Structure sub-factor of Liquidity "to focus primarily on risks to a bank's funding structure from short-term liabilities and the run risk of different types of deposits."[29] Although we broadly support a focus on short-term liabilities and run risk for these purposes, the proposal would inappropriately rely to a significant extent on the LCR requirements and associated LCR disclosures despite the relatively limited application of these requirements.

At a fundamental level, the LCR does not apply universally across banks. In the U.S., the LCR applies to fewer than two dozen banks and does not apply to many banks with between $100 billion to $250 billion in total consolidated assets or any bank below the $100 billion threshold. Even among banks subject to the LCR, requirements vary. For example, a Category IV bank with $50 billion or more in average weighted short-term wholesale funding is subject to an outflow adjustment percentage of 70 percent and a Category III bank with less than $75 billion in average weighted short-term wholesale funding is subject to an outflow adjustment percentage of 85 percent. The U.S. banking agencies have indicated that reduced requirements are appropriate for smaller and less complex banks based on an expectation that these banks "should be able to address their liquidity needs under a stress scenario in a shorter period of time."[30] Despite this limited and varied scope of application, the proposed changes would base ratings to a significant extent on LCR measures as if they were required in full, and would then impose different treatment depending on whether banks disclose the relevant LCR measures and, by extension, whether banks are subject to the LCR. In addition, methodologies regarding aspects of the LCR differ across banks, notably with respect to defining the scope of operational deposits. Consistent with the comments above regarding capital, the Liquidity and Funding Structure subfactor should produce consistent results across banks with similar liquidity profiles, reflecting the different regulatory requirements to which banks are subject.

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27 Bill Nelson, *I Don't Think the LCR Means What You Think It Means* (Oct. 22, 2021), *available at* https://bpi.com/wp-content/uploads/2021/10/I-Dont-Think-the-LCR-Means-What-You-Think-It-Means-Final.pdf.

28 Proposal, p. 41.

29 Proposal, p. 3.

30 Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, *Changes to Applicability Thresholds for Regulatory Capital and Liquidity Requirements*, 84 Fed. Reg. 59,230, 59,254 (Nov. 1, 2019).

We also are concerned about the potential qualitative adjustments to the Funding Structure and Liquidity sub-factors, which are opaque and insufficiently supported. It is particularly unclear how Moody's may implement the proposed qualitative adjustments in light of data availability constraints as banks not subject to the LCR may not be willing or able to provide the granular breakouts required by the LCR. Given that the LCR does not apply consistently across banks and does not apply at all to banks with less than $100 billion in total consolidated assets, banks across the spectrum will not publicly disclose LCR metrics in a consistent manner. The proposal does not address how Moody's would determine these sub-factor scores in the absence of collecting nonpublic data elements from individual banks.

C. The Liquid Resources sub-factor score should incorporate operational readiness concepts.

The proposal provides that Moody's expects banks "to have a robust and timely plan to access contingent liquidity to meet its needs at any point", which "typically includes the presence of pre-pledging tests such as readying borrowing agreements across its asset classes and portfolios, or testing discount window access with small and frequent transactions."[31] Under the proposal, a bank that does not have "an adequate level of pre-positioned or eligible assets" or "a well-developed and tested plan for accessing contingent liquidity even with the existence of eligible assets" may be subject to downward adjustment to the Liquid Resources sub-factor score.[32]

We broadly support incorporating into the Moody's ratings both pre-positioned or eligible assets for contingent liquidity as well as a tested plan to access contingent liquidity, including with respect to discount window advances. As reflected in the 2023 banking stress, it is important for banks to engage in both pre-positioning and testing to demonstrate operational readiness to access sources of contingent liquidity, particularly during a stress event.[33] The proposal's methodology should also take into account the overall size of a bank for purposes of any assessment of the level of pre-positioned assets of a particular bank.

IV. The evaluation of IRRBB under the bank rating methodology should not rely solely on an EVE metric.

The proposal would evaluate a bank's interest rate risk in the banking book ("IRRBB") based on "the estimated impact of a given interest rate shock (typically, a parallel shift in the yield curve) on the bank's economic value of equity (EVE)."[34] Under the proposal, Moody's may "adjust the Asset Risk sub-factor score downward where a 100 basis point shift in the yield curve across the major currencies used by a bank would be expected to result in an EVE loss of more than 5% of the bank's TCE; or where the impact of a 200 basis point shift in the yield curve across the major currencies used by a bank would be expected

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31 Proposal, p. 42.

32 Proposal, p. 42.

33 Letter to Ann E. Misback, Secretary of the Board of Governors of the Federal Reserve System, *Request for Information and Comment on Operational Aspects of Federal Reserve Bank Extensions of Discount Window and Intraday Credit (Docket No. OP-1838)* (Dec. 9, 2024), *available at* https://bpi.com/wp-content/uploads/2024/12/BPI-Comment-Letter-RFI-on-Operational-Aspects-of-Federal-Reserve-Bank-Extensions-of-Discount-Window-and-Intraday-Credit.pdf.

34 Proposal, p. 28.

to result in an EVE loss of more than 15% of the bank's TCE."[35]

We broadly support incorporating some consideration of IRRBB as one component of the revised methodology in light of the well-documented issues with interest rate risk management that resulted in the failure of SVB. However, the methodology should not rely heavily on the EVE metric or associated assumptions based on EVE for purposes of measuring IRRBB.

In general, EVE models that banks deploy are not standardized and the underlying assumptions may differ significantly across banks based on differences in balance sheets, business models, and risk management practices. In the context of quantitative ratings determinations, it is difficult to use the EVE metric to compare IRRBB levels across banks, including because some banks do not manage IRRBB based on an EVE metric or may consider EVE as merely one aspect of its overall interest rate risk management. In that regard, there is insufficient justification for adjusting the Asset Risk sub-factor scores downward as a result of EVE losses arising out of 100 basis point or 200 basis point shifts. Similar issues arise with respect to evaluating IRRBB based on net interest income sensitivity metrics, which also depend on the underlying assumptions and methodologies.

In broad terms, it will be important for Moody's and banks to work together to formulate an appropriate methodology to assess interest rate risk in a manner that may be applied consistently and transparently across banks.

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The Bank Policy Institute appreciates the opportunity to comment on the proposal. If you have any questions, please contact the undersigned by email at brett.waxman@bpi.com or by phone at (347)-237-7368.

Respectfully submitted,

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[35] Proposal, p. 28.