January 31, 2014

Via Electronic Mail

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Docket No. R-1466
RIN 7100 AE-03

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
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Docket ID OCC-2013-0016
RIN 1557 AD 74

Re: Notice of Proposed Rulemaking—Liquidity Coverage Ratio: Liquidity Risk Measurement, Standards, and Monitoring

Ladies and Gentlemen:

We appreciate the opportunity to respond to the proposed rules (the "Proposal")[1] issued by the Board of Governors of the Federal Reserve System (the "Federal Reserve"), the Federal Deposit Insurance Corporation ("FDIC"), and the Office of the Comptroller of the Currency ("OCC") (collectively, the "Agencies") to establish quantitative liquidity standards based on the liquidity coverage ratio ("LCR") framework (the "Basel LCR Framework")[2] established by the Basel Committee on Bank Supervision ("BCBS"). The Proposal comprises two sets of rules. One set jointly proposed by the Agencies would establish an LCR requirement (the "Full LCR") for banking organizations with $250 billion or more in total consolidated assets or $10 billion or more in on-balance sheet foreign exposure as well as any subsidiary depository institution with

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[1] *Liquidity Coverage Ratio: Liquidity Risk Measurement, Standards, and Monitoring*, 78 Fed. Reg. 71,818 (Nov. 29, 2013).

[2] Basel Committee on Banking Supervision, *Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools* (Jan. 2013), *available at* http://www.bis.org/publ/bcbs238.pdf.

total assets of $10 billion or more of such organizations. We refer to organizations that would be subject to the Full LCR under the Proposal as "Full LCR Banking Organizations." The Federal Reserve also proposed a modified LCR (the "Modified LCR") that would apply to bank holding companies and savings and loan holding companies that have at least $50 billion in total consolidated assets but are not Full LCR Banking Organizations. We refer to organizations that would be subject to the Modified LCR under the Proposal as "Modified LCR Banking Organizations."[3]

The undersigned institutions are regional banking organizations with total consolidated assets of between $57 billion and $361 billion, as of September 30, 2013. Our institutions are traditional banking organizations, focused on domestic business activities, whose sizes are modest in relation to both the U.S. banking sector and U.S. economic activity. For example, each of the undersigned, as of September 30, 2013, had a share of national deposits under 3%, total consolidated assets, as of that same date, that represented less than 3% of U.S. GDP, and in the aggregate, had fewer assets than the single largest U.S.-based Global Systemically Important Bank identified by the Financial Stability Board ("G-SIB").[4]

The crisis demonstrated the critical role of liquidity in protecting individual institutions and the broader financial sector. We, therefore, support the fundamental objectives of the Proposal and the Basel LCR Framework. These include, among other things, promoting the resilience of banking organizations, improving the banking sector's ability to absorb shocks arising from financial and economic stress, and improving the measurement and management of liquidity risk.

The purpose of this letter is to focus on several aspects of the Proposal that are particularly problematic and to provide alternative approaches that achieve regulatory objectives, while helping avoid unintended and adverse consequences to the financial system. As discussed in detail below, our most important recommendations are that the Agencies—

- Modify the Proposal so that regional banking organizations would be required to calculate the LCR on a monthly (rather than a daily) basis. Our organizations have less complex and volatile funding profiles than larger and more complex organizations, which makes a monthly calculation more appropriate for our organizations. In addition, developing systems capable of calculating the LCR on a daily basis presents a significant challenge and expense for our organizations given that our organizations are not currently subject to the Federal Reserve's detailed fourth generation ("4G") daily liquidity reporting requirements.

[3] Bank holding companies and savings and loan holding companies that are, or have a significant percentage of their assets held by, insurance companies, and savings and loan holding companies that have significant commercial operations would not be subject to either the Full LCR or the Modified LCR.

[4] Financial Stability Board, *2013 Update of Group of Global Systemically Important Banks (G-SIBs)* (Nov. 11, 2013), *available at* http://www.financialstabilityboard.org/publications/r_131111.pdf (updating the Financial Stability Board's list of G-SIBs using year-end 2012 data and the BCBS's updated methodology published in July 2013).

- Harmonize the scope of the Full LCR with the Federal Reserve's proposed complex institution liquidity monitoring report (FR 2052a) so that all regional banking organizations are subject to the Modified LCR (rather than the Full LCR). The proposal itself recognizes that the Modified LCR is appropriate for organizations that are less complex in structure, less reliant on riskier forms of market funding, have simpler balance sheets, and pose less risk to the financial system. As discussed further below, all of the undersigned organizations—including those that are subject to the advanced approaches for risk-based capital purposes—meet these criteria.

- Appropriately reflect the nature of deposits placed by state and local governments, as well as other collateralized deposits, by (i) exempting them from the requirement to "unwind" the deposit relationship in calculating the adjusted cap on high-quality liquid assets ("HQLA"), and (ii) revising the outflow assumptions required for public fund deposits to properly reflect the observed behavior of state and local government depositors during times of economic stress.

- Recognize the proven liquidity value and observed price behaviors, even in times of severe stress, of obligations issued by the U.S. government sponsored enterprises ("GSEs") by either including such obligations as Level 1 liquid assets or modifying the structure of the 40% cap on Level 2 liquid assets so that the liquidity value of additional GSE obligations is not completely disregarded, but may be considered subject to increasing haircuts and a higher overall cap.

- Modify the criteria necessary for a deposit to be recognized as an "operational deposit" to properly reflect the nature and characteristics of deposits maintained in connection with cash management, clearing, and custody services. The Proposal would unintentionally exclude deposits which in fact have stable properties and also would introduce compliance and supervisory challenges which could not practically be met.

Part I of this letter provides an overview of regional banking organizations and data demonstrating that our organizations have liquidity profiles that are significantly less complex and volatile than larger and more complex banking organizations; Part II addresses our concerns related to the proposed daily calculation requirement and the scope of the Full LCR relative to regional banking organizations; Part III addresses comments and recommendations related to the proposed requirements for HQLA and the proposed outflow assumptions; and Part IV discusses additional concerns related to the Proposal and includes items we respectfully request the Agencies clarify in the final rule.

Our organizations also participated in the development of the joint comment letter submitted by The Clearing House Association L.L.C., the American Bankers Association, the Securities Industry & Financial Markets Association, the Financial Services Roundtable, the Institute of International Bankers, the International Association of Credit Portfolio Managers and the Structured Finance Industry Group (the "Joint Trade Association Comment Letter").[5] We support the comments and concerns reflected in the Joint Trade Association Comment Letter,

[5] Letter to the Agencies from the Joint Trade Associations (Jan. 31, 2014).

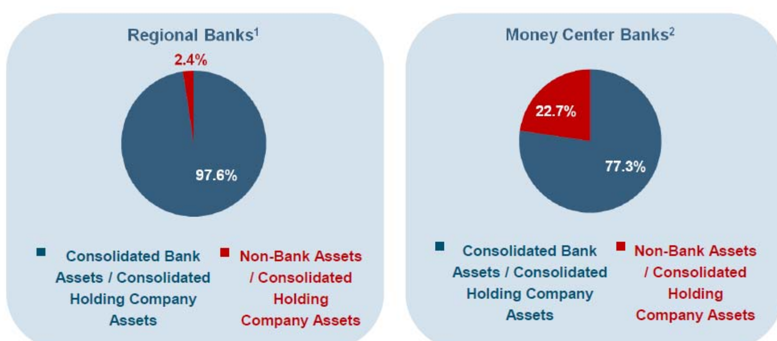
and the comments and recommendations in this letter are intended to supplement those contained in the Joint Trade Association Comment Letter.

I. Background on Regional Banks

In order to put our comments in perspective, we believe it is important to first understand the significant differences between regional banking organizations and larger, more complex banking organizations. We believe it is critical for the Agencies to keep these real differences in mind when implementing the Basel LCR Framework and other regulatory initiatives. The Basel LCR Framework was developed for internationally active banking organizations with complex structures and funding sources. Our organizations are not internationally active and do not present the complex liquidity risks the LCR was intended to address. As demonstrated by the below data, our organizations are less complex in structure, have simpler balance sheets and funding profiles, and are less reliant on riskier and more volatile forms of short-term funding than larger and more complex organizations (such as the G-SIBs).

Relative to larger and more complex organizations (such as the G-SIBs), our organizations have relatively simple organizational structures. Our organizations primarily focus on providing traditional retail and commercial banking products and services, and have only limited trading and capital markets operations. Broker-dealers and other nonbank operations comprise only a small portion of our organizations' overall operations. Rather, the vast majority of our organizations' business operations and consolidated assets are in our insured depository institution subsidiaries, and our organizations do not present systemic risks to the U.S. or global financial system.[6] *See Figure 1,* below.

<u>Figure 1</u>



Source: SNL

[1]Regional Banks include: USB, COF, PNC, BBT, STI, FITB, RF, KEY, MTB, CMA, HBAN, TD, BBVA, Citizens (the bank vs. non-bank split for BBVA, TD, and Citizens is derived from their U.S. bank holding companies)

[2] Money Center Banks include: JPM, BAC, C, and WFC

Q4 2012

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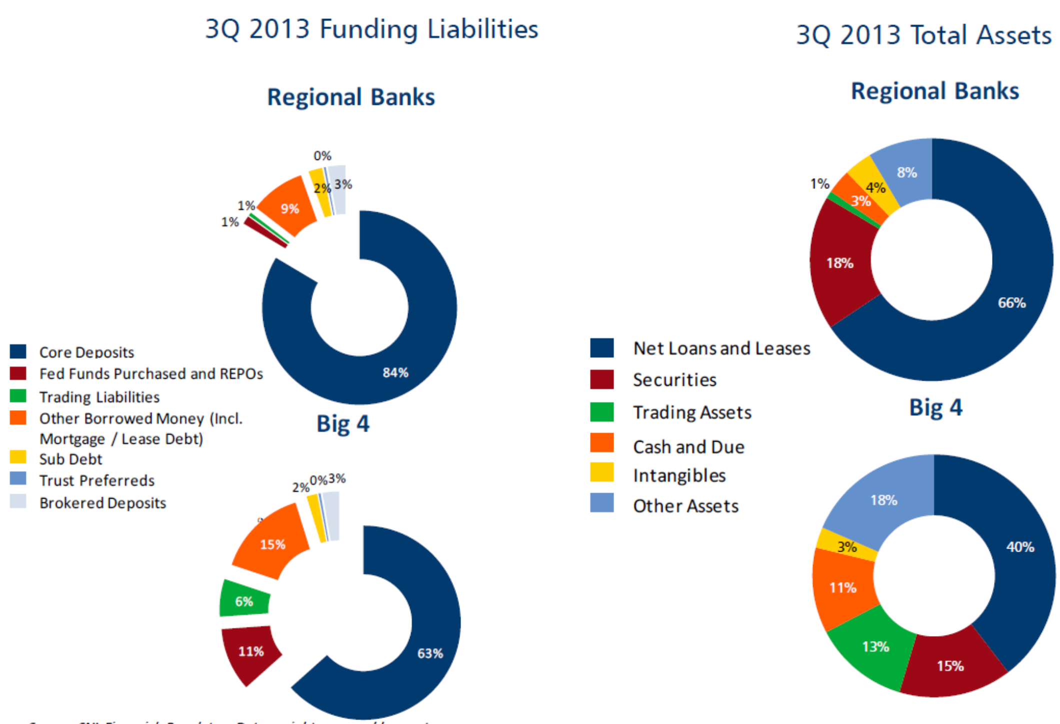
[6] The joint Federal Reserve and FDIC resolution plan rules implicitly recognize that regional banks are simpler, and less likely to pose systemic risk upon failure, than larger and more complex organizations. Each of our organizations has less than $100 billion in total nonbank assets and was part of the third and last round of resolution plan filers. *See, e.g.*, 12 C.F.R. §§ 243.3(a)(1)(iii) and 381.3(a)(1)(iii).

As a result, should our organizations experience liquidity pressures, the vast majority of our operations would be able to access ordinary course sources of liquidity available to depository institutions without the need for the type of extraordinary liquidity measures taken during the financial crisis under section 13(3) of the Federal Reserve Act to provide liquidity to <u>nonbank</u> entities.

Our organizations also rely primarily on core sources of funding, i.e., deposits, and do not rely to a significant degree on potentially volatile, short-term sources of market funding. *See Figure 2*, below. For example, our organizations engage only to a limited extent in repurchase, reverse repurchase, or other securities financing transactions. As a result of having simpler and more stable funding profiles, liquidity inflows and outflows of our organizations generally are more stable and predictable than larger and more complex organizations. Thus, our liquidity risks are easier for our management and supervisors to monitor and manage.

<u>Figure 2</u>



Source: SNL Financial, Regulatory Data; weight-averaged by assets

Notes: Big 4 banks include JPM, BofA, Citi, Wells Fargo; Regional Banks include US Bank, PNC, SunTrust, BB&T, Regions, Fifth Third, Key, M&T.; Consumer Deposits includes NOW and Other Transactional accounts, MMDA and Other Savings, Retail Time, Jumbo Time, Non Interest Bearing, and Deposits in Foreign Offices.

The limited foreign operations of our organizations further limit the complexity of our organizational structures and funding profiles. Therefore, unlike larger and more complex banking organizations with significant foreign operations, concerns about cross-jurisdictional liquidity mismatches or liquidity being trapped in foreign jurisdictions are not material issues for our organizations.

With this background, we now turn to our comments on the Proposal.

II. Proposed Daily Calculation Requirement, Scope of Application of the Full LCR, and Related Concerns

A. <u>The Daily Calculation Requirement Is Unnecessary and Unduly Burdensome for Regional Banking Organizations</u>

The Proposal would require both Full LCR Banking Organizations and Modified LCR Banking Organizations to calculate their liquidity coverage ratio on a daily basis as of a set time communicated to their primary Federal supervisor in writing. The daily calculation requirement is both (i) unnecessary for regional banks; and (ii) unduly burdensome for our organizations to implement, especially in light of the January 1, 2015, date the Agencies have proposed for implementation of that requirement.

As the data provided above in Part I illustrates, our organizations do not present the same funding complexity and liquidity risks as larger and more complex banking organizations, such as G-SIBs. Regional banking organizations do not rely to a significant extent on more volatile, short-term sources of wholesale funding. This results in liquidity inflows and outflows that are more stable and predictable than those of larger and more complex organizations. Accordingly, regional banking organizations' liquidity risks are easier for management and supervisors to monitor and manage through traditional means. We believe these facts make a daily calculation unnecessary for regional banking organizations.

The difference in liquidity risk profiles between our organizations and the G-SIBs is already recognized by the Federal Reserve in its current and proposed liquidity reporting framework. Specifically, we understand that the Federal Reserve currently requires only G-SIBs—but not other banking organizations—to provide detailed daily liquidity reporting under the Federal Reserve's 4G liquidity reporting program. In addition, the Federal Reserve's proposed liquidity monitoring framework also recognizes the different liquidity profiles and reporting capabilities of regional banking organizations and G-SIBs.[7] Under the proposed FR 2052 reporting framework, only G-SIBs would be subject to the daily complex institution liquidity monitoring report (the FR 2052a). Regional banking organizations, on the other hand, would be subject to <u>monthly</u> liquidity reporting on the FR 2052b.

Moreover, calculating the ratio on a daily basis would require extensive systems our organizations currently do not have in place. Implementing and adequately testing those systems would be very challenging, expensive, and time consuming, and such costs are not outweighed by the benefits in light of our organizations' less complex liquidity risk profiles. As noted above, our banking organizations are not subject to the Federal Reserve's current daily liquidity reporting requirements, nor are our organizations within the scope of the Federal Reserve's proposed daily complex institution liquidity monitoring report (FR 2052a). Banking organizations that are subject to the 4G liquidity report, and that received notice that they would be subject to daily reporting on the FR 2052a, have had considerable lead time, relative to our banking organizations, to prepare for and build the systems capable of supporting a daily

[7] *Proposed Agency Information Collection Activities; Comment Request*, 78 Fed. Reg. 57,634 (Sep. 19, 2013).

calculation. The burden associated with developing and testing systems capable of supporting the daily calculation is significantly magnified by the Agencies' proposed implementation date, i.e., all banking organizations subject to the Proposal would be subject to the daily calculation requirement starting on January 1, 2015. Whether banking organizations not currently subject to daily liquidity reporting could develop and appropriately test the systems necessary to support a daily calculation between now and the proposed implementation date is questionable at best, and may not even be possible.[8]

For the foregoing reasons, we recommend that the Agencies harmonize the required frequency of calculating the ratio with the reporting frequency the Federal Reserve already has proposed for its liquidity monitoring report. Using those criteria, the requirement to calculate the ratio on a daily basis would apply to G-SIBs, whereas our organizations and other regional banking organizations would be subject to a monthly calculation.[9] Applying the daily calculation requirement in this manner would appropriately reflect the differences between regional banking organizations and larger and more complex banking organizations in the context of the LCR. Monthly calculation frequency for regional banking organizations also would be consistent with the Federal Reserve's proposed rules to implement the enhanced liquidity standards required under section 165 of the Dodd-Frank Act, which would require covered companies to conduct internal liquidity stress tests at least monthly.[10]

If the Agencies nonetheless decide to maintain the daily calculation requirement even for regional banking organizations, we respectfully request that banking organizations that presently are not subject by the Federal Reserve to daily liquidity reporting requirements be given additional time to implement a daily calculation requirement. In such circumstances, we believe

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[8] As part of its analysis of the Proposal under the Unfunded Mandates Reform Act of 1995, the OCC estimated that Full LCR Banking Organizations supervised by the OCC (21 national banks and federal savings associations) would each spend approximately 2,760 hours during the first year the rule is in effect, primarily to develop the systems to collect and process the data needed to calculate the LCR. *See Proposal*, at 71,854. It is unclear from the OCC's estimate whether the agency took into account that some Full LCR Banking Organizations it supervises currently are not subject to a daily liquidity reporting requirement in developing this estimate. Nonetheless, we believe that the OCC's figure greatly underestimates the burden associated with implementing the daily calculation requirement by many multiples.

[9] The Agencies could leverage the supervisory process in situations where heightened monitoring of liquidity might be warranted for non-G-SIBs. The simpler liquidity risk profile of our organizations would make such monitoring effective. Adopting the monthly calculation approach we recommend also would necessitate conforming changes to the proposed notification procedures banking organizations would be required to adhere to if their ratio falls below the level required. As proposed, the remediation requirements are tied to the requirement to calculate the ratio on a daily basis. We believe that, for organizations that calculate and report the ratio monthly, the shortfall notification procedures should apply if the organization's monthly report indicates the organization fell below the required level. Similarly, the requirement for a mandatory corrective action plan should apply if the organization remains below the required level for 2 consecutive months, unless the Agencies determine that a corrective action plan is needed sooner.

[10] *See Enhanced Prudential Standards and Early Remediation Requirements for Covered Companies; Proposed Rule*, 77 Fed. Reg. 594 (Jan. 5, 2012) (hereinafter *Enhanced Prudential Standards Proposal*).

that delaying the implementation of the daily calculation requirement until 2017, at a minimum, for banking organization not already subject to daily liquidity reporting requirements would be appropriate. Regardless of what calculation frequency the Agencies require in the final rule, we respectfully ask that our organizations be given sufficient time to implement any LCR-related reporting requirements the Agencies may seek to implement. We believe that LCR-related reporting requirements should not take effect until 2017, at the earliest, and that our organizations should, at a minimum, be given one year following adoption of any LCR reporting standards to build and test the necessary reporting infrastructure.[11]

B. <u>All Regional Banking Organizations Should Be Subject to the Modified LCR</u>

The proposal indicates that the Full LCR is intended to apply to internationally active banking organizations that, should they fail as a result of liquidity stress, would have significant systemic impact. However, the Agencies have proposed to apply the Full LCR to any banking organization with $250 billion or more in total consolidated assets or $10 billion or more in on-balance sheet foreign exposure, as well as the subsidiary depository institutions of such organizations with total assets greater than $10 billion. This threshold inappropriately captures certain of the undersigned regional banking organizations ("Covered Regional Banks")[12] even though the business models, operations and funding profiles of these Covered Regional Banks are much more similar to the organizations that would be subject to the Modified LCR, than to the organizations (such as the G-SIBs) sought to be covered by the Full LCR.

In this regard, the Federal Reserve's Modified LCR proposal specifically recognizes that the Modified LCR is appropriate for organizations that—

- Are less complex in structure, less reliant on riskier forms of market funding, and have simpler balance sheets;

- Have liquidity risks that are easier for management and supervisors to monitor and address quickly in a stressed scenario; and

- Would likely not have as great a systemic impact as larger, more complex companies should they experience liquidity stress.[13]

As the data in Appendix 1 demonstrates, the undersigned Covered Regional Banks meet each of these criteria and, thus, are more appropriately covered by the Modified LCR. These data compare several key metrics related to balance sheet composition, funding profile and

[11] In order to facilitate the use of existing data by our organizations for any reporting requirement tied to the LCR, we believe any such requirements must allow for sufficient time following the "as of" date to collect, aggregate, and submit the necessary data. For example, for a monthly reporting requirement, our organizations should not be required to submit such a report until, at the earliest, the 20th day of the calendar month following the "as of" date.

[12] These are Capital One Financial Corp., The PNC Financial Services Group, Inc., TD Bank US Holding Co., and U.S. Bancorp.

[13] *Proposal*, at 71,846.

international activity for Covered Regional Banks versus the same metrics for (i) G-SIBs; and (ii) all banking organizations that we estimate would be subject to the Modified LCR under the Proposal. As these data indicate, the balance sheet, funding profile and international activities of Covered Regional Banks are very different from the balance sheet, funding profile and international activities of the G-SIBs. On the other hand, this same data demonstrates that the balance sheet, funding profile and international activities of Covered Regional Banks are very similar to that of the banking organizations that would be subject to the Modified LCR. To highlight just a few of these metrics:

- While the average ratio of Total Trading Assets to Total Assets of the G-SIBs is 16%, the same average ratio is less than 1% for Covered Regional Banks and less than 1% for all Modified LCR Banking Organizations;

- While the average ratio of Derivative Contracts (notional value) to Total Assets of the G-SIBs is 2,549%, the same average ratio is only 57% for Covered Regional Banks and 38% for all Modified LCR Banking Organizations;

- While the average reliance on wholesale funding ratio (as calculated under the methodology used by the OCC as part of its Canary supervisory system) for the G-SIBs is 46%, the same average ratio is only 23% for Covered Regional Banks and 24% for all Modified LCR Banking Organizations;

- While the average ratio of Core Deposits to Total Assets for the G-SIBs is only 29%, the same average ratio is 70% for Covered Regional Banks and 62% for all Modified LCR Banking Organizations; and

- While the average ratio of Average Foreign Loans to Average Total Loans of the G-SIBs is 18%, the same average ratio is only 1% for Covered Regional Banks and <1% for Modified LCR Banking Organizations.

We believe that these data clearly demonstrate that it would be more appropriate—both from a regulatory and a competitive equality standpoint—for all regional banks, including Covered Regional Banks, to be covered by the Modified LCR.

As noted above, the Federal Reserve already has recognized that regional banking organizations have simpler and less complex liquidity profiles than the G-SIBs. For example, only G-SIBs are subject to the current daily 4G liquidity reporting framework, and only G-SIBs would be subject to the Federal Reserve's proposed FR 2052a daily complex institution liquidity monitoring report.[14] We believe this same line should be used for purposes of determining the scope of the Full LCR and the Modified LCR. Under this approach, the Full LCR would apply to U.S.

[14] In addition to the differences in reporting frequency between the FR 2052a (daily for G-SIBs) and the FR 2052b (monthly for bank holding companies with $50 billion or more in total consolidated assets that are not G-SIBs), the FR 2052b report also would require more limited and streamlined reporting than the FR 2052a.

banking organizations that have been designated as G-SIBs,[15] and other less complex banking organizations, including Covered Regional Banks, would be subject to the Modified LCR.[16]

We believe modifying the Full LCR in this manner is consistent with safety and soundness considerations, the Basel LCR Framework, and the direction provided by Congress in Section 165 of the Dodd-Frank Act.[17] In this regard, Covered Regional Banks would continue to be subject to the same quantitative liquidity risk management requirements (i.e., the Modified LCR) that apply to other, comparable regional banking organizations. In addition, Covered Regional Banks would continue to be subject to the Federal Reserve's enhanced liquidity standards established under section 165 of the Dodd-Frank Act,[18] and the Agencies' liquidity risk management expectations set forth in the Interagency Policy Statement on Funding and Liquidity Risk Management.[19] Notably, the alternative scope for the Full LCR we propose also would be the least costly alternative, according to the OCC's analysis under the Unfunded Mandates Reform Act.[20]

We also believe the Agencies have the flexibility under the Basel LCR Framework to expand the scope of the Modified LCR in the manner we recommend.[21] The Basel LCR Framework does not define "internationally active banks" or otherwise define the scope of the framework. As the data in Appendix 1 illustrates, Covered Regional Banks are not internationally active and would not have significant systemic impact should they fail as a result of liquidity stress. Exercising the flexibility the Agencies have under the Basel LCR Framework to define anew which organizations should be considered "internationally active" is particularly appropriate considering that the Agencies are proposing to implement the first quantitative liquidity standards in the United States.

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[15] This scope would also be consistent with the scope of the Agencies' proposed enhanced supplementary leverage ratio, which would apply only to G-SIBs as a result of the $700 billion total consolidated asset or $10 trillion in assets under custody thresholds. *Regulatory Capital Rules: Regulatory Capital, Enhanced Supplementary Leverage Ratio Standards for Certain Bank Holding Companies and Their Subsidiary Insured Depository Institutions*, 78 Fed. Reg. 51,101 (Aug. 20, 2013).

[16] If, nonetheless, the Agencies determine to continue to apply the Full LCR to some regional banking organizations, we believe that, at a minimum, modifications to the manner in which the Full LCR would be applied to subsidiary depository institutions are necessary. These are discussed further in Part II.D. below.

[17] Section 165(a)(2) provides for any enhanced prudential standards to be tailored based on a firm's riskiness, complexity, size and financial activities, as well as other relevant risk-related factors. 12 U.S.C. § 5365(a)(2).

[18] *See Enhanced Prudential Standards Proposal supra* note 10.

[19] 75 Fed. Reg. 13,656 (Mar. 22, 2010).

[20] *See supra* note 8.

[21] The Basel frameworks, including the Basel LCR Framework, provide national authorities responsibility for identifying those organizations that should be considered "internationally active." *See Basel LCR Framework*, ¶ 164; *see also* BCBS, *International Convergence of Capital Measurement and Capital Standards: A Revised Framework – Comprehensive Version* (June 2006), *available at* http://www.bis.org/publ/bcbs128.htm.

C. Modified LCR's 21-Day Stress Period Does Not Appropriately Align with the Calendar Month Cycle of Bank Customer Activity

We support the use of cumulative net cash outflows over the stress period in the Modified LCR (rather than peak cumulative net cash outflows). The approach of using cumulative outflows over the period is appropriate for regional banking organizations because our funding profiles are simpler and less volatile than larger, more complex organizations and, thus, do not present the same concerns about potential intra-month maturity mismatches that the Agencies indicate was a motivator of the proposed peak outflow approach under the Full LCR.[22]

However, the Modified LCR's 21-day stress period makes calculating and managing the ratio more challenging because most bank customer activity follows a calendar-month cycle. This is especially true for customer activity at regional banking organizations, which primarily focus on providing traditional retail and commercial banking products. Given that customer activity is rooted in a calendar-month cycle, our organizations also manage maturities and refinancing with a monthly view in mind. For example, our organizations can accurately estimate the time of the month when large volumes of customer payments will be received and can time debt maturities based on that monthly time frame. The 21-day forward-looking stress period required under the Modified LCR would consistently omit key recurring payment activity that occurs on the calendar-month cycle and force our organizations to manage cash flows in an abnormal manner.

Accordingly, we respectfully ask the Agencies to modify the proposed 21-day stress period under the Modified LCR to instead provide for a calendar-month stress period.[23] Under this approach the Modified LCR would be calculated using the Federal Reserve's proposed outflow and inflow assumptions (based on 70% of the proposed outflow and inflow rates under the Full LCR) over the course of a calendar-month projection period. Modifying the projection period in this way would better align the Modified LCR with established internal liquidity management and external regulatory and financial reporting cycles. We believe retaining the Modified LCR's proposed outflow and inflow rates after modifying the projection period would appropriately scale the assumptions under the Full LCR to regional banking organizations that present less liquidity risk.[24] Adopting the calendar-month approach would also decrease the complexity of the LCR calculation for regional banking organizations.

[22] *See Proposal*, at 71,833.

[23] We also believe that the Full LCR should follow a calendar-month projection period, rather than the proposed 30-calendar day approach.

[24] Scaling the outflow assumptions applicable to regional banks would be particularly appropriate considering that, as noted above, regional banking organizations predominantly operate through depository institution subsidiaries that have access to ordinary course liquidity sources. These resources would make a liquidity stress event easier for regional banking organizations to manage without the need for extraordinary liquidity support.

D. Proposed Requirement to Calculate the LCR at Both the Consolidated Holding Company Level and the Subsidiary Bank Level is Unnecessary

The Proposal would require bank holding companies subject to the Full LCR to calculate the ratio at both the consolidated level and at each consolidated depository institution subsidiary that itself would be subject to the Full LCR or has $10 billion or more in total consolidated assets. For the reasons discussed above, we believe that regional banks should not be subject to the Full LCR. However, if the Full LCR is applied to any regional banking organization, we believe that important modifications are necessary to how the rules apply to the separate entities within a bank holding company.

First, under the Proposal, excess liquidity at the holding company would be disregarded for purposes of calculating the ratio at the depository institution level. Disregarding excess parent liquidity does not recognize the requirement, previously imposed in regulation by the Federal Reserve[25] and now codified in the Dodd-Frank Act,[26] that a bank holding company serve as a financial source of strength to its subsidiary depository institutions. The Agencies should revise the Proposal so that a bank holding company, at its election, can count excess HQLA at the bank holding company in the store of HQLA at a depository institution subsidiary.[27] Doing so would be consistent with the principle that the holding company act as a source of strength for its subsidiary depository institutions and with prudent liquidity management principles.

Second, in requiring individual subsidiary depository institutions to calculate the Full LCR, the Proposal would not adequately recognize the relationship between consolidated depository institutions that are subsidiaries of the same holding company (so called "sister banks"). The Proposal should be revised so that a depository institution, in calculating its Full LCR, is permitted to count in its HQLA amount any excess HQLA held by an affiliated insured depository institution.[28] Doing so would be consistent with the principles set forth by the so-called "sister bank exemption" in Section 23A of the Federal Reserve Act[29] and with the principles established by Congress in the cross-guaranty liability provisions of the Federal Deposit Insurance Act.[30]

Third, the Proposal would limit the amount of excess HQLA held by consolidated subsidiaries that can count towards the parent company's HQLA stock to amounts that would be available to the parent company "during times of stress without statutory, regulatory, contractual, or supervisory restrictions . . . ."[31] It is impossible, however, to predict what statutory, regulatory,

[25] *See* 12 C.F.R. § 225.4 and App. C.

[26] *See* §616, codified at 12 U.S.C. § 1831o-1.

[27] We would appreciate the opportunity to discuss with the Agencies how best to calculate excess HQLA at the parent bank holding company level.

[28] Such excess HQLA amount could, of course, only be counted by one of the sister banks.

[29] 12 U.S.C. § 371c(d)(1)(C).

[30] 12 U.S.C. § 1815(e).

[31] Section __.20(e)(3)(B) of the *Proposal*.

supervisory or other additional restrictions may apply to a depository institution subsidiary in some future hypothetical stress period. We, therefore, respectfully request that the Agencies clarify that in applying this limitation, a bank holding company is required only to apply those statutory, regulatory, and contractual restrictions that are in effect at the time of calculation.

III. Requirements for Assets to Qualify as HQLA and Standardized Outflow Amounts

A. Public Sector and Certain Corporate Trust Deposits Required to Be Collateralized with HQLA Should Not Be Treated Like Repurchase Agreements

The treatment under the Proposal of deposits placed by states and municipalities, which, under state law must be collateralized[32] (so called "preferred deposits"),[33] as well as certain corporate trust deposits that often are collateralized,[34] is punitive and more stringent than required under the Basel LCR Framework. As a result, banking organizations likely would have to limit the amount of preferred deposits and collateralized corporate trust deposits they accept, further reduce the interest paid on preferred deposits and corporate trust deposits, or eliminate earnings credits extended to state and municipal depositors.[35] We believe the treatment of preferred deposits and collateralized corporate trust deposits under the Proposal is unintended and inappropriate and, therefore, urge the Agencies to modify the treatment of these deposits in the final rule.

The Proposal requires that the caps on Level 2 liquid assets (i.e., 40% of total HQLA for Level 2 and 15% for Level 2B) be calculated both before and after giving effect to an assumed unwind of any HQLA-for-HQLA transactions (e.g., repurchase agreements or collateral swap transactions).[36] The lower of the two HQLA amounts would be used to calculate the ratio. The Agencies explain in the Proposal that the adjusted excess HQLA requirement is intended to prevent a banking organization from manipulating its HQLA portfolio by engaging in

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[32] *See, e.g.*, Ohio Rev. Code §§ 135.18, 135.181, and 135.37. Under Ohio law, a bank cannot accept deposits of public moneys from a political subdivision or county, unless the bank pledges collateral for the repayment of all public moneys to be deposited in the institution. The law also specifies the types of securities eligible to be pledged as collateral under that requirement, including, among other types of securities, GSE securities, Treasury securities, and U.S. government agency securities. *See generally* Ohio Rev. Code § 135.18.

[33] *See* 12 U.S.C. § 1813(m)(4).

[34] Pursuant to OCC regulations, a national bank may place funds for which the bank is a fiduciary on deposit in the bank (such deposits are often referred to as "self-deposits"). *See* 12 C.F.R. § 9.10. Those regulations also require that the bank set aside collateral to secure self-deposits to the extent they are not insured by the FDIC. *Id.*

[35] Preferred deposits are generally placed in connection with banking services states or municipalities seek to obtain from banks (e.g., treasury management services). States and municipalities generally do not pay directly for these services but instead receive earnings credits for the deposits placed with the bank.

[36] The measures are referred to in the Proposal as the "unadjusted excess HQLA amount" and the "adjusted excess HQLA amount," respectively.

transactions, such as repurchase or reverse repurchase transactions, that would allow the organization to quickly convert Level 2 assets to Level 1 assets.[37]

The Proposal, however, would treat deposits collateralized with, for example, GSE obligations, in the same manner as repurchase agreements for purposes of the adjusted excess HQLA calculation.[38] As the example included as Appendix 2 illustrates, applying the proposed unwind requirement to preferred deposits and collateralized corporate trust deposits could well result in situations where the transactions result in a negative HQLA amount. Moreover, under the Proposal, collateralized deposits would be subject to <u>both</u> an outflow assumption (generally 15%, when secured by GSE obligations) <u>and</u> the adjusted excess HQLA provision that would require banking organizations to assume that the transaction is unwound.

While we support the Agencies' goal of preventing banking organizations from manipulating their stock of HQLA, preferred deposit and collateralized corporate trust deposits simply do not raise those concerns. In contrast to repurchase agreements or other collateral swaps, preferred deposits represent a part of long-term banking relationships with state and municipal governments. These deposits are generally placed with banks in connection with other services the public sector customer seeks to obtain from the bank, e.g., payments and receivables treasury management services, and are not susceptible to the type of short-term gaming the Agencies seek to prohibit. These relationships generally are established through a request for proposal process. Similarly, collateralized corporate trust deposits also represent part of a broader customer relationship.[39]

Accordingly, neither type of collateralized deposit raises the concerns about manipulation the Agencies seek to address with the requirement to calculate the adjusted excess HQLA amount. The Agencies should be aware that under the Proposal preferred deposits would lose their economic value to the banking organizations that hold them. If banking organizations subject to the Proposal have to turn away these deposits, public sector depositors may face difficulties as it is unlikely that smaller banks could provide the types of banking services public sector

[37] *Proposal*, at 71,831.

[38] The Proposal defines the "adjusted level 2A liquid asset amount" as the amount equal to 85 percent of the fair GAAP value of all level 2A liquid assets that would be held by the banking organization upon the unwind of, among other things, any "secured funding transaction." *See* §__.21(f)(2). The term "secured funding transaction" is defined to include any transaction that gives rise to a cash obligation of the banking organization to a counterparty that is secured under applicable law by a lien on specifically designated assets owned by the banking organization that gives the counterparty, as holder of the lien, priority over the assets. *See* §__.3. While preferred deposits would fall into this broad definition, it appears that this result may have been unintended. For example, in describing the reasons for, and application of, the adjusted HQLA cap, both the Basel LCR Framework and the Proposal focus on repurchase, reverse repurchase, and securities financing transactions—not preferred deposits or collateralized corporate trust deposits. *See Proposal*, at 71,831; *Basel LCR Framework*, ¶ 48.

[39] These relationships include, for example, trustee or agency services provided in connection with the issuance of debt, or in connection with a variety of other types of corporate, commercial, securities-related or litigation-related transactions involving a financing, security or escrow arrangement. Trustee and agency engagements undertaken by a bank's corporate trust department generally are nondiscretionary in nature and are governed by detailed administrative agreements.

customers need or that smaller banks could absorb the deposit base (based both on their size and the lack of collateral available at smaller banks). For these reasons, we request that the Agencies clearly exclude preferred deposits and collateralized corporate trust deposits from the requirement to unwind HQLA-for-HQLA transactions in the final rule. After excluding them from the unwind requirement, these deposits would continue to be subject to an outflow assumption.

B. Outflow Assumptions for Preferred Deposits Secured with FHLB Letters of Credit

State law restricts the manner of collateral acceptable to secure deposits of public funds, and banks generally pledge GSE obligations or FHLB letters of credit ("LCs") as collateral. Under the proposal, the outflow assumptions for preferred deposits secured by GSE obligations would be 15%,[40] but it is unclear from the Proposal what outflow rate would apply to FHLB LC-secured preferred deposits.[41]

We believe that the outflow assumption for preferred deposits secured with FHLB LCs should be the same as that for preferred deposits secured with GSE obligations (15%). This would properly reflect the behavior of public sector deposits even in times of stress. For example, the aggregate peak 90-day outflow rate of public sector deposits observed at National City Bank, Washington Mutual Bank, and Wachovia Bank—three institutions that experienced extreme stress prior to being acquired—during the recent crisis was approximately 15.9%.[42] While the historical data does not break out preferred deposits by collateral types, we have no reason to believe that the behavior of a public sector depositor would differ based on whether deposits are secured with GSE obligations or an FHLB LC. GSE obligations and FHLB LCs both qualify equally as eligible collateral under applicable state law and both represent a claim backed by a GSE.

Accordingly, we respectfully ask the Agencies to clarify in the final rule that the outflow rate applicable to preferred deposits secured with FHLB LCs is the same as the outflow rate for preferred deposits secured with GSE obligations (15%). Doing so would more accurately reflect the historical behavior of state and municipal depositors in times of economic stress. If the agencies are unwilling to do so, the Agencies, at the least, should clearly address the treatment of preferred deposits secured with FHLB LCs in the final rule and confirm that FHLB LC-secured preferred deposits that satisfy the operational deposit criteria receive an outflow rate of no higher than 25%.

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[40] *See* §__.32(j)(1)(ii) of the *Proposal*.

[41] Because FHLB LCs are not considered HQLA under the Proposal, it would appear that a preferred deposit secured with an FHLB LC could be treated as "unsecured wholesale funding" with an assigned outflow rate of 40% under §__.32(h)(1)(ii), or 25% if the preferred deposit meets the "operational deposit" criteria.

[42] *Source*: FDIC – Statistics on Depository Institutions (data between March 31, 2007, and June 30, 2008).

C. Agencies Should Revise the Proposed Treatment of GSE Obligations to More Appropriately Recognize Their Proven Liquidity Value

GSE obligations are a primary tool for liquidity risk management for U.S. banking organizations and currently comprise a significant amount of liquidity portfolios because they reliably trade in deep and liquid markets. While the Agencies acknowledge that securities issued and guaranteed by the GSEs consistently trade in very large volumes and generally have been highly liquid, including during times of stress,[43] the Proposal would treat these assets as Level 2A liquid assets subject to the 40% cap on total Level 2 assets and a 15% haircut.

We believe that the treatment of GSE obligations under the Proposal does not adequately reflect the proven liquidity value and observed price behaviors of GSE obligations, even in times of severe stress. Moreover, the characterization of GSE obligations as Level 2A assets is inconsistent with the enhanced liquidity standards the Federal Reserve proposed under section 165 of the Dodd-Frank Act, which would classify GSE obligations as fully liquid.[44] The treatment of GSE obligations in the Proposal has the potential to negatively impact the availability and pricing of residential mortgages in the United States.

Accordingly, we urge the Agencies to reconsider the treatment of GSE obligations in the final rule—particularly in light of the fact that the GSEs currently operate under the conservatorship of the Federal Housing Finance Agency and continue to receive capital support from the U.S. Treasury under the terms of the Preferred Stock Purchase Agreements—to more appropriately reflect the proven liquidity value of these securities. We support the recommendation made in the Joint Trade Association Comment Letter to treat GSE obligations as Level 1 liquid assets.[45] While the GSEs receive support from the U.S. government, GSE obligations are effectively guaranteed by the full faith and credit of the U.S. government, which would make their treatment as Level 1 liquid assets consistent with the Proposal and the Basel LCR Framework.

However, should the Agencies decide not to treat GSE obligations as Level 1 liquid assets, we recommend modifying the structure of the 40% cap on Level 2 liquid assets to avoid a situation where any amount of GSE obligations over the 40% cap is accorded no liquidity credit—a position that is not realistic in light of the demonstrated liquidity behavior of GSE obligations during the financial crisis. Under this alternative approach, the treatment of GSE obligations up to the 40% cap would remain unchanged from the Proposal. Rather than receiving no recognition, however, GSE obligations in excess of the 40% cap would be eligible as Level 2A liquid assets, subject to a haircut that would increase as the proportion of GSE obligations to total HQLA increases.

The following table illustrates how the modified cap we propose would apply:

[43] *Proposal*, at 71,827.

[44] *See supra* note 10.

[45] *See* Joint Trade Association Comment Letter, Section IV.A.1.

Haircut Percentage based on GSE % of HQLA - Example		
GSE % of HQLA	Additional Haircut	Total Haircut
Greater than 40% - less than 50%	5%	20%
50% - less than 60%	25%	40%
60% - less than 70%	45%	60%
70% - less than 80%	65%	80%
80% - 100%	85%	100%

Importantly, this graduated cap approach would not allow a banking organization to rely exclusively on GSE obligations to satisfy its requirement to maintain a sufficient amount of HQLA to meet its projected outflows. The graduated cap we recommend would allow GSE obligations to comprise no more than 80% of a banking organization's total stock of HQLA. We believe such a graduated cap on GSE obligations would more appropriately reflect the proven liquidity value of GSE obligations, without allowing banking organizations to over-rely on this class of liquid assets.

D. Requirements for Recognizing Certain Deposits as "Operational Deposits"

We agree with the Agencies' objectives regarding operational deposits, as discussed in the preamble to the Proposal.[46] However, the Proposal adds several specific criteria that a deposit would have to satisfy in order to be treated as an "operational deposit." These criteria are ambiguous, are inconsistent with how operational deposits actually function, in many cases are not required under the Basel LCR Framework, and would not further the purposes of the Proposal. In addition, the requirements for recognizing certain deposits in connection with cash management, clearing, or custody services as "operational deposits" are unnecessarily cumbersome and should be streamlined. As a result, the Proposal's treatment of operational deposits may unnecessarily narrow the approach in a way that would fail to recognize the scope of operational deposits, could lead to inconsistent application of the approach among banking organizations subject to the Proposal, and, importantly, runs the risk of causing the vast majority

[46] Operational deposits are expected to have a lower impact on an institution's liquidity during times of liquidity stress because the likelihood of significant withdrawals within the stress period would be reduced due to legal or operational limitations. The Proposal provides the example of a company that relies on an institution for payroll processing services. Such a customer would not be likely to move that banking relationship to another institution during a liquidity stress because the customer's need for stability in providing payroll are unaffected by stresses in the broader financial markets. *Proposal*, at 71,841.

of operational deposits to not qualify for the outflow assumptions specified under the Basel LCR Framework. Accordingly, we ask that the Agencies remove certain criteria that are fundamentally inconsistent with how operational deposits function or are unnecessary or duplicative, and adopt the revised language recommended in the Joint Trade Association Comment Letter to clarify certain other criteria.

We highlight our most significant concerns below:

1. Termination Provisions

In order to qualify as an operational deposit under the Proposal, the deposit must:

> *"be held pursuant to a legally binding written agreement, the termination of which is subject to a minimum 30 calendar-day notice period or significant termination costs are borne by the customer providing the deposit if a majority of the deposit balance is withdrawn from the operational deposit prior to the end of a 30 calendar-day notice period."*[47]

While there usually are substantial costs for a company to move an operational relationship to another institution, the deposits that support these relationships typically are not subject to specific contractual significant termination costs. Moreover, such deposits are, by definition, held in a transaction account that does not require any notice for withdrawal of deposits. This criterion instead should focus on the agreement relating to the operational services associated with the deposit. As such, the termination provision of the services agreement—rather than any related deposit account agreement—should either require 30-calendar days' notice or result in termination costs to the customer for terminating the relationship prior to the end of the notice period. We believe it is important that the final rule (like the Basel LCR Framework) recognize that the qualifying switching costs to the customer would include not just the termination costs under the operational services agreement, but also would include other costs that a customer moving the relationship would incur, whether incurred internally or from other third parties (such as costs related to information technology and other operational changes/and or expenses). In our experience, operational service customers would have substantial switching costs, given the nature of the operational services being provided.

2. Average Balance Volatility

A further requirement in order for a deposit to qualify as an operational deposit under the Proposal is that "[t]here must not be significant volatility in the average balance of the deposit."[48] However, the balance of an operational deposit, by definition, fluctuates as funds are used to meet operational needs of the depositor. Accordingly, we are concerned that this criterion could disqualify deposits based on normal variations in balances due to the nature of the operational services provided, rather than due to other factors, such as the customer's perception of the financial condition of the banking organization. Ordinary course changes in balances needed for

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[47] Section __.4(b)(1) of the *Proposal*.

[48] Section __.4(b)(2) of the *Proposal*.

the related operational services should not preclude treatment as operational deposits. While the balance of any single account may fluctuate from day to day, the value of an operational deposit is found in the aggregated diversified portfolio of such deposits. Finally, any concern that changes in operational deposit balances are not related to the underlying operational services would be addressed by the proposed exclusion of "excess deposits," making this requirement unnecessary. We therefore ask that the Agencies remove the proposed "significant volatility" requirement.

3. No Incentive to Maintain Excess

We are concerned that the proposed requirement that, in order to qualify as an operational deposit, the deposit account must not "be designed to create an economic incentive for the customer to maintain excess funds" in the account is both inconsistent with established industry practice and unnecessary.[49] Many operational deposit account relationships provide that clients can offset their expenses related to operational services through an earnings credit rate, or "ECR." This is an industry practice that helps clients offset fees and charges related to operational services. Moreover, any concern that changes in operational deposit balances are not related to the underlying operational services would again be addressed by the exclusion of any "excess deposits" from the scope of an operational deposit. As an alternative to removing this requirement, we respectfully ask the Agencies to acknowledge in the final rule that the ECR is not the type of incentive to maintain excess funds the Proposal intends to prohibit. We believe the intention of this criterion is well founded, but believe the Agencies should only prohibit economic incentives that fall outside the scope of helping offset fees for the very operational services which make operational deposits stable.

4. Methodology for Determining Excess Amounts

The Proposal would disqualify from operational deposit status "any excess amount" that the banking organization cannot demonstrate, using a "methodology" developed by the banking organization, is "empirically linked" to the operational services.[50] While we support the exclusion of excess amounts, we believe banking organizations should not have to make this demonstration on a deposit-by-deposit basis. We believe that too granular of a focus would have material practical implications both on the ability of banking organizations to produce the necessary information and the Agencies' ability to supervise compliance. It is industry practice for banking organization that are significant providers of operational services to assess the stability and nature of their operational deposits on an aggregated basis, generally by customer type or service category. This reflects the normal day-to-day flow of operational activities within client accounts, which results in variability that can accurately be measured only on an aggregated basis. We therefore respectfully ask that the Agencies confirm in the final rule that the empirical assessment of excess operational deposits may be applied on a portfolio basis, rather than on a deposit-by-deposit or customer-by-customer basis.

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[49] Section __.4(b)(5) of the *Proposal*.

[50] Section __.4(b)(6) of the *Proposal*.

E. Agencies Should Revise the Outflow Amounts for Credit and Liquidity Facilities Provided to Bank Customer Securitized Credit Facilities and Clarify the Definition of "Special Purpose Entity" to Exclude Operating Companies

Under the Proposal, banking organizations would be required to apply a 100% outflow rate for the undrawn amount of all committed credit and liquidity facilities extended to special purpose entities ("SPEs") that could be drawn within the stress period.[51] The Agencies indicate that this treatment is appropriate because SPEs are sensitive to emergency cash and backstop needs in a short-term stress environment, such as those experienced by structured investment vehicles ("SIVs") during the recent financial crisis.[52] We are concerned that the Agencies' proposed definition of SPE is overly broad and would capture a wider range of entities than the Agencies intended. Moreover, the proposed 100% outflow rate for undrawn commitments to all SPEs would apply unduly punitive treatment to traditional banking relationships with customers that are conducted through SPEs.

Specifically, the proposed SPE definition would appear to capture certain types of operating companies that are established for, and operate to achieve, a specific purpose. Such entities could include, for example, individual limited liability companies that are formed to develop, operate, or manage specific real estate assets, such as an apartment building, hotel or office complex. While we do not believe the Agencies intended to cover operating companies with the proposed definition, we respectfully request that the Agencies modify the definition of SPE in the final rule to clarify that operating companies are not the type of companies intended to be captured by the SPE definition.

We are also concerned that the Proposal does not appropriately recognize that transactions where, for example, an SPE acts as the borrower in a securitized credit facility established to finance the receivables originated by a commercial company sponsoring the SPE are fundamentally different from the types of transactions involving SPEs that give rise to the concerns the Agencies seek to address in the Proposal. For example, bank customer securitization credit facilities[53] are established as substitutes for, or complements, to traditional secured and unsecured revolving credit facilities provided to a bank customer. The bank customer accesses financing under the facility by selling financial assets (e.g., receivables generated in the normal course of the customer's business) to an SPE that it sponsors.[54] Draws on a bank customer securitization facility are strictly limited by a borrowing base of eligible financial assets (e.g., receivables), which are generated through the bank customer's business. In times of economic stress, reduced sales naturally would result in fewer receivables to support

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[51] Section __.32(e)(vi) of the *Proposal*.

[52] During that period, the Agencies note, many SPEs experienced severe cash shortfalls, as they could not rollover debt and had to rely on borrowing and backstop lines. *Proposal*, at 71,838.

[53] For these purposes, a "bank customer securitization facility" has the same meaning as described in detail in the comment letter to the Agencies from the Structured Finance Industry Group ("SFIG") and the Securities Industry & Financial Markets Association ("SIFMA"). Letter from SFIG and SIFMA to the Agencies (Jan. 31, 2014), Section I.A.

[54] The SPE structure isolates the collateral from the bank customer's bankruptcy and credit risk.

funding under the facility. In other words, the borrowing base would adjust to reflect decreased receivables and a customer's ability to draw on the facility would, therefore, be constrained during times of economic stress. The Proposal, however, would apply a 100% outflow rate for undrawn commitments to even these types of SPEs.

We believe that the outflow amount for a bank customer securitization credit facility should match the outflow amount that would apply to a credit facility extended directly to the relevant bank customer. Accordingly, we respectfully request that the Agencies revisit the proposed treatment of SPEs established in connection with bank customer securitization facilities in the final rule and adopt the modifications to the Proposal recommended by SFIG and SIFMA in their comment letter.[55] The "look through" approach recommended by the SFIG and SIFMA would appropriately harmonize the outflow treatment for bank customer securitization facilities with the outflow amounts for credit commitments extended to the underlying bank customer.

F. Agencies Should Eliminate the 10% Outflow Assumption for Brokered Deposits Provided by a Retail Customer or Counterparty Which Mature Later Than 30 Calendar Days from the Calculation Date

Under the Proposal, banking organizations are required to assume an outflow of 100% for brokered deposits that are provided by a retail customer or counterparty and mature 30 calendar days or less from the calculation date. As a result, banking organizations would be required to hold enough HQLA to cover the entire amount of retail brokered deposit balances maturing within the 30-day stress period. In addition, a 10% outflow amount would apply to brokered deposits that are provided by a retail customer or counterparty and that mature later than 30 calendar days from the calculation date. While we understand the Agencies' concern regarding the stability of brokered deposits, the requirement to recognize a cash outflow amount equal to 100% of balances maturing within 30 calendar days should sufficiently address the Agencies' concerns and, by itself, establishes a very conservative approach. Moreover, the proposed additional 10% outflow requirement does not recognize the comprehensive contractual limitations on a customer's ability to withdraw funds prior to the scheduled maturity date.

The standardized brokered retail term deposit contract places severe restrictions on a retail customer's ability to arbitrarily withdraw his or her funds prior to the contractual maturity of the term deposit. In fact, early withdrawal of any brokered retail term deposit is only permitted under the contract in the event of death or adjudication of incompetence of a depositor. Outside of those very limited situations, customers are not permitted to withdraw funds prior to the contractual maturity of the instrument.

Accordingly, we respectfully request that the Agencies eliminate the 10% outflow amount for brokered deposits provided by a retail customer or counterparty which mature later than 30 calendar days from the calculation date.

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[55] *See generally* Letter to the Agencies from SFIG and SIFMA, Section I.A.

G. Removal of Unnecessary Conditions on U.S. Agency and GSE Obligations to Be Considered HQLA

Eligible Level 1 liquid assets include both Treasury obligations and other obligations issued, or unconditionally guaranteed as to timely payment of principal and interest, by other U.S. government agencies (such as the Government National Mortgage Association) backed by the full faith and credit of the U.S. government ("Agency obligations").[56] However, Agency obligations (unlike Treasury securities) can be included in HQLA only if the banking organization demonstrates that the securities are "liquid and readily-marketable," meaning that they are traded in an active secondary market with (i) more than two committed market makers; (ii) a large number of non-market maker participants on the buying and selling side; (iii) timely and observable market prices; and (iv) a high trading volume.[57] GSE obligations also can be included in the stock of HQLA only if the banking organization can demonstrate that these assets meet the conditions to be deemed "liquid and readily-marketable."[58]

We believe the requirement for banking organizations to demonstrate that Agency and GSE obligations are "liquid and readily-marketable" is unnecessary because these obligations clearly meet these requirements. For example, Agency obligations—like Treasury securities—are backed by the full faith and credit of the United States, and we believe all obligations backed by the full faith and credit of the United States are, in fact, liquid and readily-marketable. In addition, the data included in the Joint Trade Association Comment Letter clearly demonstrates that GSE obligations also are liquid and readily-marketable.[59] Accordingly, we recommend that the Agencies revise the Proposal to eliminate the requirement that banking organizations demonstrate that Agency and GSE obligations are "liquid and readily-marketable," as this requirement is unnecessary.

H. Outflow Amount for Securities where the Banking Organization is the Primary Market Maker in Its Own Securities

The Proposal would require a banking organization to recognize an outflow amount associated with its own debt securities if the banking organization is the "primary market-maker" for the securities.[60] While we recognize that, during times of stress, a banking organization acting as the primary market-maker in its own debt securities may be called upon to provide liquidity to the market and to repurchase its debt securities, we support the concerns raised in the Joint Trade Association Comment Letter that the proposed outflow rates in these circumstances are too high. The actual volume of any repurchases made by a banking organization may be lower than the proposed outflow rates because investors may not be willing to have the banking organization repurchase the debt securities during a stress scenario at a price which would result in the

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56 *See generally* §__.20(a) of the *Proposal*.

57 Section __.20(a)(4) of the *Proposal*.

58 Section __.20(b) of the *Proposal*.

59 GSE obligations include obligations issued or guaranteed by Fannie Mae and Freddie Mac, including residential mortgage-backed securities guaranteed by Fannie Mae or Freddie Mac.

60 Section __.32(i) of the *Proposal*.

investor recognizing a significant loss. We, therefore, believe that the Agencies should adopt the recommendation in the Joint Trade Association Comment Letter to allow each banking organization to determine its own approach rather than mandating uniform outflow rates that are too high.[61]

I. Treatment of Securities Issued by State and Municipal Governments

Under the Proposal, a banking organization would receive no credit for any securities issued by state and municipal governments because these securities do not qualify as HQLA. However, under the Basel LCR Framework, securities issued by state and municipal governments that qualify for 20% risk weighting under the regulatory capital framework and that meet certain other criteria would qualify as Level 2A assets (subject to a 15% haircut and the 40% cap on all Level 2 assets).[62] The Proposal's treatment of state and municipal obligations will strongly discourage banking organizations from holding state and municipal securities in their investment portfolios, shrinking the market for these securities and increasing the cost of credit for states and municipalities.

We believe the Agencies should permit state and municipal securities to qualify as Level 2A liquid assets to the same extent as permitted under the Basel LCR Framework. We note that in its recent report on appropriate definitions of HQLA, the European Bank Authority ("EBA") recommended including certain bonds issued by European local government institutions as HQLA.[63] The EBA recommended that such assets could be included as HQLA if the obligations have (i) an external credit rating of "ECAI 2" or above; (ii) a minimum issue size of € 250 million; and (iii) a maximum time to maturity of 10 years. A similar approach could be used, modified as appropriate for the U.S. market, for identifying the state and local government securities eligible for inclusion in Level 2A liquid assets under the LCR Framework.[64]

J. Recognition of the Federal Home Loan Bank System as an Important Source of Liquidity

The Proposal would not recognize the proven ability of depository institutions to obtain secured advances from the FHLBs even in times of stress. The unused capacity to obtain advances from an FHLB is not included in the definition of HQLA, nor is such capacity recognized as a potential cash inflow in the denominator. Facilities provided by the FHLBs, which are unique to the United States, are an important source of liquidity for depository institutions. Throughout the recent financial crisis, the FHLBs proved to be a reliable source of liquidity support for U.S.

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[61] *See* Joint Trade Association Comment Letter, Section III.D.

[62] *Basel LCR Framework*, ¶ 52.

[63] EBA, *Report on appropriate uniform definitions of extremely high quality liquid assets (extremely HQLA) and high quality liquid assets (HQLA) and on operational requirements for liquid assets under Article 509(3) and (5) CRR* (Dec. 20, 2013), *available at* http://www.eba.europa.eu/-/eba-publishes-reports-on-liquidity.

[64] For example, in light of the prohibition in section 939A of the Dodd-Frank Act on the use of credit ratings, the external credit rating criteria could be modified to require that the obligations be "investment grade" as defined in the Agencies' risk-based capital rules.

banks. Accordingly, we believe the Agencies should recognize the proven liquidity value of the FHLBs by allowing at least some portion of a subsidiary depository institution's unused FHLB borrowing capacity to be counted as a cash inflow.

IV. Additional Concerns and Requests for Clarification

A. Requirements for Determining Maturity

The Proposal requires a banking organization to assume that it would not exercise an option that would allow the organization to extend the maturity of any obligation it has issued.[65] It is not clear from the Proposal, however, whether the Agencies also intend to require a banking organization to assume that it exercises call options that allow it to close out a wholesale funding instrument, such as long-term debt, in advance of the contractual maturity date. Debt instruments with embedded call options, e.g., a 30-day call option, are purchased by sophisticated institutional investors and provide the issuing banking organization with an important degree of funding flexibility.

Requiring a banking organization to assume that these types of options are exercised is counterintuitive, as it would imply that the banking organization must disadvantage itself in a stress scenario by, for example, assuming that it exercises a 30-day call option embedded in certain of its debt instruments, thereby accelerating such obligations. In addition, there is no market expectation that a banking organization would exercise such a call option on its long-term debt in a stress environment. We, therefore, respectfully ask that the Agencies clarify in the final rule, or the preamble thereto, that a banking organization would not be required to assume that it would exercise call options embedded in wholesale funding instruments issued by the banking organization.

B. Proposed Definition of "Regulated Financial Company" Poses Certain Operational Challenges

Under the proposal, securities and other obligations issued by a "regulated financial company" or another financial sector entity would be excluded from HQLA entirely. Similarly, funding provided by a "regulated financial company" generally is subject to the highest outflow assumptions under the Proposal. In the context of the HQLA definition, the Proposal explains that this treatment of "regulated financial companies" and other financial sector entities is meant to address "wrong way risk." While we support the Agencies' efforts to address financial sector interconnections in the Proposal, the definition of "regulated financial company" is problematic. Specifically, the second element of that definition would include any company that must be included in the organizational chart of a banking organization subject to the Proposal, as reported on the Federal Reserve's Form FR Y-6 and reflected on the National Information Center website.[66]

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[65] Section __.31(a)(1)(ii) of the *Proposal*.

[66] http://www.ffiec.gov/nicpubweb/nicweb/NicHome.aspx.

Because of the breadth of investments that must be reported on the FR Y-6, this prong of the definition is overly broad and operationally burdensome without providing meaningful benefit and should be eliminated from the definition of "regulated financial company." The FR Y-6 is intended to annually provide the Federal Reserve with data to allow supervisory staff to monitor the activities of holding companies, ensure that their activities are conducted in a safe and sound manner, and monitor the permissibility of the investments made by holding companies. Accordingly, the FR Y-6 is an expansive form that is meant to capture a substantial range of activities and investments of depository institution holding companies. For example, the FR Y-6 requires a depository institution holding company to include a company on its FR Y-6 organizational chart even if it owns only 5% of a class of the company's voting securities. It must also include merchant banking investments that are reportable on the Federal Reserve's Form FR Y-10.

The scope of the FR Y-6 means that companies will be treated as "regulated financial companies" even where a banking organization's investment may be significantly below the threshold at which the company would be consolidated for financial reporting purposes or even considered to be "controlled" by the banking organization for purposes of the Bank Holding Company Act. A company in which a banking organization has a minority and possibly noncontrolling interest would not necessarily have the kind of "links" with the banking organization that would be "sufficiently significant" to warrant treatment of such company as a regulated financial company. Moreover, merchant banking investments of banking organizations that are financial holding companies engage in commercial activities and the banking organization is prohibited from routinely managing or operating the company (except for a limited period of time in exceptional circumstances). Thus, we believe it would be inappropriate to characterize these portfolio companies as a regulated financial company.

C. Treatment of Vault Cash in HQLA

Cash, whether held in branches or ATMs, represents the most liquid of assets and ultimately provides the funding for deposit withdrawals. The intrinsic liquidity value of cash is recognized in the Basel LCR Framework, which includes "coins and banknotes" as Level 1 HQLA,[67] and the Federal Reserve's proposed enhanced liquidity requirements, which includes "cash" in the definition of "highly liquid assets."[68] The Proposal, however, strangely does not include cash in the definition of HQLA. We believe this result was unintentional.

Specifically, the Proposal allows a banking organization's "Reserve Bank balances" to be included in its HQLA as a Level 1 liquid asset.[69] However, this term is generally defined to include only certain types of balances held by, or on behalf of, the bank at a Federal Reserve Bank. Thus, the amount of a bank's vault cash cannot be included in HQLA under the Proposal even though such vault cash can be used to satisfy the bank's reserve requirement under the Federal Reserve's regulations.[70]

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[67] *Basel III Framework*, ¶ 50(a).

[68] *See* § 252.51(g) of the *Enhanced Prudential Standards Proposal*, *supra* note 10.

[69] *See* § __.20(a)(1) of the *Proposal*.

[70] *See* 12 C.F.R. § 204.5(a)(1).

We believe that vault cash should count towards a banking organization's HQLA as a Level 1 liquid asset. Indeed, it would be anomalous if cash itself did not constitute HQLA, given that a core guiding criterion for HQLA is whether the asset is "easily and immediately convertible into cash with little or no loss of value during a period of liquidity stress."[71] Accordingly, we respectfully request that the Agencies modify the Proposal to provide that vault cash (as defined in section 204.2(k)(1) of the Federal Reserve's Regulation D)[72] is a Level 1 liquid assets. This definition would include U.S. currency held at the relevant banking organization's proprietary ATMs, as well as U.S. coin and currency in transit to a Federal Reserve Bank (or a correspondent depository institution), or in transit from a Federal Reserve Bank (or a correspondent depository institution) if the bank has been charged for the shipment.

D. <u>Clarifying the Treatment of Letters of Credit and Other Contingent Funding Obligations</u>

The Proposal does not appear to address whether the rules would apply to letters of credit not backing liquidity facilities and other similar contingent funding obligations. We do not believe that such contingent funding obligations should be subject to an outflow assumption under the final rule given that these contingent funding obligations represent credit events generally tied to the performance of a third party, rather than liquidity events related to stress of a particular banking organization or in the financial markets. The Basel LCR Framework provides national authorities with discretion to determine the run-off rates for these kinds of contingent funding obligations.[73] We, therefore, respectfully ask that the Agencies clarify in the final rule that letters of credit not backing liquidity facilities and other similar contingent funding obligations are not subject to any outflow assumption under the rules.

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71 *See Proposal*, at 71,823.

72 12 C.F.R. § 204.2(k)(1).

73 *Basel III Framework*, ¶¶ 134 and 140.

V. Conclusion

The undersigned thank the Agencies for the opportunity to comment on the Proposal and respectfully ask for consideration of the recommendations and suggestions in this letter. If you have any questions regarding the content of this letter or would like more information on the same, please do not hesitate to contact any of the individuals listed in *Attachment 1* appended hereto.

Sincerely,

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Comerica Bank
Fifth Third Bancorp
Huntington National Bank
KeyCorp
M&T Bank Corporation
The PNC Financial Services Group, Inc.
RBS Citizens Financial Group
Regions Financial Corp.
SunTrust Banks, Inc.
TD Bank US Holding Company
Union Bank, N.A.
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<u>Attachment 1</u>

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Appendix 1: Balance Sheet and Funding Profile Data for Covered Regional Banks

Figure 3—Balance Sheet Composition[74, 75]

	A	B	C	D	E
Banking Organizations	Net Loans & Leases / Total Assets (%)	Total Trading Assets / Total Assets (%)	Total Trading Liabilities / Total Liabilities (%)	4(k) Broker-Dealer Assets / Total Assets (%)[76]	Derivative Contracts (Notional) / Total Assets (%)
U.S. G-SIB – Average	25%	16%	7%	19%	2,549%
Covered Regional Banks – Average	58%	<1%	<1%	<1%	57%
All Modified LCR Banks – Average	63%	<1%	<1%	2%	38%

Figure 4—Funding Profile[74, 75]

	A	B	C	D	E	F
Banking Organizations	Reliance on Wholesale Funding (%)[77]	Core Deposits / Total Assets (%)	Loans / Deposits (%)	Reverse Repurchase Agreements (%)	Sec. Sold/Repo / Total Liabilities (%)	Net Short-term Liabilities/ Assets (%)[77]
U.S. G-SIB – Average	46%	29%	61%	15%	11%	-21%
Covered Regional Banks – Average	23%	70%	82%	<1%	<1%	-5%

[74] Average data is for (i) U.S. G-SIBs; (ii) the undersigned regional banking organizations that would be subject to the Full LCR under the Proposal (i.e., Capital One Financial Corp., The PNC Financial Services Group, Inc., TD Bank US Holding Co., and U.S. Bancorp); and (iii) all bank holding companies and savings and loan holding companies that we estimate would be subject to the Modified LCR.

[75] The source of all information is SNL – FR Y-9C (data as of September 30, 2013). Data reported as 'N/A' was treated as a zero for purposes of these calculations.

[76] Broker-dealer asset data are included only for broker-dealer subsidiaries of financial holding companies that engage in underwriting or dealing pursuant to section 4(k)(4)(E) of the Bank Holding Company Act, *see* line item 20.a. of Schedule HC-M to the FR Y-9C.

[77] These ratios are used by the OCC as part of its Canary supervisory system and derived using publicly available FR Y-9C/Call Report data.

Figure 4—Funding Profile[74, 75]

	A	B	C	D	E	F
Banking Organizations	Reliance on Wholesale Funding (%)[77]	Core Deposits / Total Assets (%)	Loans / Deposits (%)	Reverse Repurchase Agreements (%)	Sec. Sold/Repo / Total Liabilities (%)	Net Short-term Liabilities/ Assets (%)[77]
All Modified LCR Banks –	24%	62%	96%	3%	<1%	-8%

Figure 5—International Activity[74, 75]

	A	B
Banking Organizations	Total Foreign Deposits / Total Deposits (%)	Avg. Foreign Loans / Avg. Total Loans (%)
U.S. G-SIB – Average	28%	18%
Covered Regional Banks – Average	3%	1%
All Modified LCR Banks – Average	1%	<1%

Appendix 2: Impact of the Adjusted HQLA Cap on Preferred Deposits and Collateralized Corporate Trust Deposits

As discussed in Part III.A., the proposed requirement to unwind preferred deposits and collateralized corporate trust deposits for purposes of calculating the adjusted HQLA cap can have significant negative consequences. Below, we illustrate these consequences with a hypothetical example where an institution with $10 billion in non-maturity preferred deposits secured by $11 billion of Level 2A assets (e.g., GSE obligations).

Effect of Proposed Treatment of Preferred Deposits on Liquidity		
Assumptions	**Calculation**	**Result ($B)**
Unencumbered Level 1 Assets (a)	–	8
Unencumbered Level 2 Assets (b)	–	10
Unencumbered Level 2B Assets (c)	–	0
Level 1 Liquid Asset Amount (d)	a	8
Level 2 Liquid Asset Amount (e)	b * .85	8.5
Level 2b Liquid Asset Amount (f)	c * .5	0
Secured Funding Position is Unwound		
Adjusted Level 1 Liquid Asset Amount (g)	d – 10	–2
Adjusted Level 2 Liquid Asset Amount (h)	e + ($11B * .85)	17.85
Adjusted Level 2b Liquid Asset Amount (i)	f	0
Unadjusted Excess HQLA Calculation		
Level 2 Cap Excess Amount (j)	MAX (e + f –.6667*d, 0)	3.1664
Level 2b Cap Excess Amount (k)	MAX (f – j – .1765 * (d + e), 0)	0
Unadjusted Excess HQLA Amount (l)	j + k	3.1664
Adjusted Excess HQLA Calculation		
Adjusted Level 2 Cap Excess Amount (m)	MAX (h + i – .6667 * g, 0)	19.1834
Adjusted Level 2b Cap Excess Amount (n)	MAX (i – m – .1765 * (g + h), 0)	0
Adjusted Excess HQLA Amount (o)	m + n	19.1834
Calculation of HQLA Amount	d + e + f – MAX (l, o)	–2.6834