Ilya Beylin
Associate Professor
Seton Hall Law School
[redacted]

Chief Counsel's Office,
Attention: Comment Processing, Office
of the Comptroller of the Currency, 400
7th Street SW, Suite 3E–218,
Washington, DC 20219

Ann Misback, Secretary,
Board of Governors
of the Federal Reserve System,
20th Street and Constitution Avenue NW,
Washington, DC 20551

Jennifer M. Jones,
Deputy Executive Secretary,
Attention: Comments/Legal OES (RIN 3064–AG11),
Federal Deposit Insurance Corporation,
550 17th Street NW,
Washington, DC 20429.

July 30, 2025

Dear Sir\Madam:

This letter is a response to the request for comment on certain matters related to capital requirements applicable to banking organizations proposed by the Office of the Comptroller of the Currency (RIN 1557–AF31), Federal Reserve Board (RIN 7100–AG96) and Federal Deposit Insurance Corporation (RIN 3064–AG11).

I am a professor of business law at Seton Hall Law School, and, among other things, previously practiced in the financial institutions groups of Sullivan & Cromwell LLP and Sidley Austin LLP. My scholarship focuses on financial markets. I write in my personal capacity, and the views expressed in this letter represent only my personal views. The views expressed in this letter are not the views of Seton Hall University, Seton Hall Law School, or anyone else associated with Seton Hall.

I write to generally oppose the proposed revisions to the leverage ratios applicable to banking organizations (including insured depository institutions). I agree that the current capital requirements are mis-calibrated. However, I believe that the proposed changes would only further undermine capital standards.

With this background, I provide responses to certain specific questions:

Question 1: What are the advantages and disadvantages of replacing the fixed two percent eSLR buffer standard applicable to a GSIB with a buffer standard equal to 50 percent of a GSIB's method 1 risk-based surcharge? What other modifications should the Board consider for purposes of ensuring that the eSLR buffer standard generally does not serve as the binding capital constraint for GSIBs, and why?

Replacing the fixed two percent (2%) eSLR buffer with a buffer equal to 50 percent of a GSIB's method 1 risk-based surcharge would ignore assets treated as risk free under the risk-weighting rules, including much sovereign debt. This would make the eSLR insensitive to a wide swath of low-risk but not riskless operations, requiring the banking regulators to focus additional attention on these areas in more discretionary supervision (e.g., stress tests).

Specifically, I believe current capital rules incorrectly approach sovereign debt, treating most sovereign debt as risk free and ignoring the real risks of holding sovereign debt. This would need to be recalibrated before applying risk-based charges in leverage ratios.

As background, the current risk-weighting approach to sovereign debt ignores substantial risk. The Basel Committee on Banking Supervision (BCBS) recommends the use of credit ratings in risk-weighting sovereign debt.[1] However, the Dodd-Frank Act makes it impermissible to use credit ratings in regulation.[2] Instead, U.S. banking regulators primarily base risk weights of sovereign debt on (a) whether the issuer is a member of the OECD, and (b) the issuer's country risk classification as reported by the OECD, if any.[3] The OECD risk classification process specifically exempts Euro area countries and OECD members from risk assessments if they are "high income".[4] In turn, U.S. risk-weighted capital rules treat the absence of reporting as a determination that an OECD country is risk-free.[5] This leads to the U.S. risk weights for sovereign debt being optimistic assessments of creditworthiness for the following countries: Australia, Austria, Belgium, Canada, Chile, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Japan, Korea, Latvia, Lithuania, Luxembourg, Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, United Kingdom, United States.[6] For example, as of the writing of this Article, S&P rates: Chile an A, Hungary a BBB-, Italy a BBB+, Japan an A+, Mexico a BBB, and Spain an A.[7] However all six countries are high income OECD members, so that their risk-weight under U.S. capital rules is zero percent. As a result of failing to distinguish between dozens of sovereign issuers and treating them as risk free, the U.S. capital

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[1] BCBS, *Basel III: Finalizing Post-Crisis Reforms* at 4 BIS (Dec. 2017), available at https://www.bis.org/bcbs/publ/d424.pdf. The BCBS standards do permit the U.S. approach as an accommodation to politics, but it is not the recommended approach.

[2] Sections 939 and 939A of the Dodd-Frank Act prohibit federal agencies from basing the application of regulations on credit ratings.

[3] *See, e.g.,* 12 C.F.R. § 3.2 (defining "Country risk classification (CRC) with respect to a sovereign, [as] the most recent consensus CRC published by the [OECD] as of December 31st of the prior calendar year that provides a view of the likelihood that the sovereign will service its external debt.")

[4] OECD, *Country Risk Classifications of the Participants to the Arrangement on Officially Supported Export Credits* (June 27, 2025), available at https://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/country-risk-classification/cre-crc-current-english.pdf. High income OECD members include: Australia, Austria, Belgium, Canada, Chile, Czechia, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Japan, Korea, Latvia, Lithuania, Luxembourg, Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, United Kingdom, United States. Id.

[5] 12 C.F.R. § 3.32(a)(2).

[6] As referenced below, when these assets are in the trading book, risk-based standards do take them into account. However, when they are available for sale (or being held to maturity), the risk-based approach ignores the risk of default, interest rate risk (including inflation risk), tax risk, reinvestment risk, and other sources of risk that sovereign debt is subject to.

[7] Trading Economics, *Credit Rating*, https://tradingeconomics.com/country-list/rating (last visited July 19, 2025).

rules subsidize the holding of sovereign debt. Furthermore, capital rules relatively promote investment in higher risk sovereigns (among OECD high income countries) as the debt from these issuers pays higher interest. Setting leverage ratios on the basis of the risk-based surcharge would import these distortions from the risk-based capital framework into the leverage ratio framework, exacerbating the misallocation of banking assets towards sovereign debt. Not only is this facially mis-calibrated, but it has the appearance of accommodating fiscal policies at a time of extreme deficit spending. Financial stability regulation should not serve (or appear to serve) goals of supporting fiscal profligacy.

Question 5: What would be the advantages and disadvantages of incorporating the narrow exclusion approach in any final rule, and why?

The narrow exclusion approach refers to the proposed modification of the calculation of total leverage exposure for depository institution holding companies to exclude Treasury securities that are reported as trading assets on the organizations' balance sheets and that are held at broker-dealer subsidiaries (and foreign equivalents thereof) that are not subsidiaries of a depository institution. This approach admittedly does not wholly omit the risk from these Treasury securities as the risk would still be accounted for in analysis of the trading book (and mark-to-market realization of any gains and losses). I do not know whether this approach more accurately captures the risk of Treasury holdings by broker-dealer subsidiaries, but assume for purposes of this comment letter that it does. Nevertheless, this approach is problematic because it produces a departure from BCBS standards and invites a race to the bottom in regulation. The U.S. would be on a slippery slope, and further declinations from BCBS standards could follow. At the same time, other jurisdictions could see this example as justification for departing from BCBS standards in their own ways. The harmonization of capital and other banking regulation has substantial value, which I believe exceeds any minor gains from more accurate calibration.

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I would be glad to hear from you at [redacted] to discuss these and related matters further whether via setting up a call or through correspondence.

Sincerely,

[redacted]

Professor Ilya Beylin